When Is a Commission Due?
Problems with Broker Listing Agreements

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Under traditional property law a real estate broker earns her commission when she is the procuring cause of an offer to purchase from a ready, willing, and able purchaser that matches the seller’s listing price (or is otherwise acceptable to him). Dozens of cases so hold. See, e.g., Steve Schmidt & Co. v. Berry, 228 Cal. Rptr. 689 (Ct. App. 1986); Liggett Realtors, Inc. v. Gresham, 831 N.Y.S.2d 59 (N.Y. App. Div. 2007). This reflects the common law, and similar language is usually found in printed form listing agreements.

But this rule has implications that can be quite undesirable for sellers. If a commission is earned by the mere fact of procuring the right kind of offer, then it does not matter whether a deal a broker puts together ever actually is consummated. The commission earned does not thereby become unearned if the deal falls through, perhaps because of the buyer’s breach of contract. But an ordinary seller is naturally uncomfortable with the idea of owing a commission when no sales proceeds exist to supply the payment.

The rule has another unpopular consequence: if the buyer’s offer matches the seller’s asking price (and is unconditional), then the broker’s commission is earned, whether or not the seller accepts the offer. The seller is free to change his mind and decide not to sell, but that seller nevertheless will be liable to his broker for a commission. See, e.g., East Kendall Ins., Inc. v. Bankers Real Estate Partners, 742 So. 2d 302 (Fla. Dist. Ct. App. 1999).

A Sensible Rule?
Generally, amateur sellers (that is, most homeowners) are stunned on learning that their signed listings result in the outcomes described above, but experienced sellers (as well as experienced attorneys for amateur or professional sellers) always make certain to revise their listing agreements to change the traditional commission rule. Indeed, one might wonder about the wisdom of a rule that takes unsophisticated parties by surprise and is always changed by the sophisticated ones. If rules are supposed to be efficient and fair, why is this one still on the books?

Most judicial opinions do not try very hard to explain or justify the rule, but simply refer to it as “settled.” The rule dates back to the 19th century and simply attempts to tie the broker’s function in a deal to her right to compensation from it. As the Pennsylvania Supreme Court put it:

Brokers are persons whose business it is to bring buyer and seller together. They need have nothing to do with the negotiation of the bargain. [So] a broker becomes entitled to

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his commissions whenever he procures for his principal a party with whom he is satisfied, and who actually contracts for the purchase of the property at a price acceptable to the owner.

Keys v. Johnson, 68 Pa. 42, 43 (Pa. 1871). Prof. Barlow Burke’s treatise on real estate brokerage attempts to offer a better explanation:

There is a sound rationale for this rule. For example, the vendor might add conditions and contingencies to the contract of sale not specified in the listing agreement and over which the broker has no control, and then refuse to sign the contract which the purchaser presented. In such situations, the broker’s failure to obtain a contract on the property is excusable. Absent a breach of fiduciary duty, the broker should not suffer for the vendor’s recalcitrance or cold feet.

Barlow Burke Jr., Law of Real Estate Brokers § 5.02 (2012). But that explanation seems to prove too much. An alternative to the present rule could easily say that brokers earn commissions only when and if deals close, except for cases in which the closing is prevented by the seller’s conduct. (In fact, that’s what many attorney-drafted listing agreements declare.)

Ellsworth Dobbs: A Contrary Rule

On the other hand, court opinions in perhaps a dozen states have rejected the traditional rule and held instead that a broker earns a commission only if the deal actually closes. These opinions are filled with policy explanations. In Ellsworth Dobbs, Inc. v. Johnson, 236 A.2d 843 (N.J. 1967), which started the opposing trend, the New Jersey Supreme Court said:

[F]airness requires that the arrangement between broker and owner be interpreted to mean that the owner hires the broker with the expectation of becoming liable for a commission only in the event a sale of the property is consummated, unless the title does not pass because of the owner’s improper or frustrating conduct.

When a broker is engaged by an owner of property to find a purchaser for it, the broker earns his commission when (a) he produces a purchaser ready, willing and able to buy on the terms fixed by the owner, (b) the purchaser enters into a binding contract with the owner to do so, and (c) the purchaser completes the transaction by closing the title in accordance with the provisions of the contract.

Id. at 853, 855. Ellsworth Dobbs not only created a new rule but also made it more than a default gap-filling rule that could be easily changed by the parties (that is, by the broker):

There can be no doubt that the business of the real estate broker is affected with a public interest. ... [P]ublic policy requires the courts to read into every brokerage agreement or contract of sale a requirement that barring default by the seller, commissions shall not be deemed earned against him unless the contract of sale is performed. By the same token, whenever the substantial inequality of bargaining power, position or advantage to which we have adverted appears, a provision to the contrary in an agreement prepared or
presented or negotiated or procured by the broker shall be deemed inconsistent with public policy and unenforceable.

Id. at 856, 857—58. In other states, reversing the new rule by contract may be difficult but not impossible. For example, in Tristram’s Landing, Inc. v. Wait, 327 N.E.2d 727, 731-32 (Mass. 1975), the court held that “agreements by the seller to pay a commission even though the purchaser defaults are to be scrutinized carefully. If not fairly made, such agreements may be unconscionable or against public policy.”

The Ellsworth Dobbs rule is still a minority view, with perhaps a dozen adherents, and a few states have considered and rejected it. See, e.g., Specialty Rests. Corp. v. Adolph K. Feinberg Real Estate Co., Inc., 770 S.W.2d 324, 327 (Mo. Ct. App. 1989); Fairbourn Commercial, Inc. v. American Hous. Partners, Inc., 94 P.3d 292, 294 (Utah 2004). When Ellsworth Dobbs applies, ordinarily the broker will not be entitled to a commission unless and until there is a closing of the sale. As the quotation from the opinion above shows, however, the New Jersey court thought that if the seller himself was the cause of the deal’s failure to close (“because of the owner’s improper or frustrating conduct”), the commission should be payable. Presumably this entitlement would include both cases in which the seller accepted but then breached a contract of sale and those in which the seller received an unconditional full price offer but simply refused to accept it.

A sort of surreptitious middle rule also operates in this field, when courts pay ostensible homage to the majority rule but manage to find that the circumstances justify reaching the minority Ellsworth Dobbs result instead. This is usually accomplished by finding that the parties intended to create commission liability only in the event of a closing, even if they forgot to say so. A recent California case illustrates this attitude.

**California’s RealPro Decision— Rejecting a $17 Million Offer**

In RealPro, Inc. v. Smith Residential Co., LLC, 138 Cal. Rptr. 3d 255 (Ct. App. 2012), the seller gave a listing for sale of 46.8 acres of land in Riverside County, California, at $17 million to its broker, who then put it into the local multiple listing file. RealPro, a cooperating broker, submitted an offer to purchase the property four weeks later for the asking price—$17 million, all cash. At this point the seller evidently concluded that it had set its original listing price too low, rejected the offer, and countered at $19.5 million. The buyer walked out, however, ending negotiations, and the cooperating broker (RealPro) sued the seller for its share of the promised commission.

California says it follows the traditional view that a broker earns a commission when she is the procuring cause of a ready, willing, and able purchaser that offers to buy the property on the terms set by the seller in his listing agreement. Moreover, the RealPro listing agreement said the same thing; the commission was payable if “a buyer is procured who is ready, willing and able to buy the Property at the price and on the terms stated herein, or on any other price and terms agreeable to [owner].” Id. at 258. The form used for the listing was Standard Owner-Agency Agreement for Sale or Lease of Real Property (Non-Residential), AIR Commercial Real Estate Association Form OA-1— 6/97 (1997), available on-line at [www.agentsplanet.com/pdf/150/Sale%20or%20Lease%20of%20Real%20Property.pdf](http://www.agentsplanet.com/pdf/150/Sale%20or%20Lease%20of%20Real%20Property.pdf). The opinion does not indicate that
the form was modified by the parties. Thus, RealPro was not a situation in which the traditional rule was varied by the express terms of the listing contract.

Notwithstanding these facts, the seller prevailed and was held to not have any duty to pay a commission. The California Court of Appeal thought a parade of horribles would follow a contrary construction of the contract, including an inability by the seller to accept a higher offer after a lower offer matching the asking price had already been received, potential liability for multiple commissions when several good offers were received, liability even when the purchaser had breached the contract, and discouraging buyers’ brokers from submitting lower offers. Some of these worries do raise legitimate questions. They also may be warning signs that this court has decided it is not going to let such bad consequences occur.

In RealPro, the owner had received the full price offer one month after listing the property. The common and obvious response is for such a seller to make a counteroffer at a higher price. But if the listing agreement really earns the broker a commission at the moment the offer is received, then making a counteroffer could lead to loss of a sales contract (because the purchaser can reject it) while at the same time preserving liability for a commission. That may be the logical consequence of the wording of the traditional listing agreement, but it is certainly not a sensible one from the seller’s viewpoint, because it forces him to accept an offer that could probably be better.

This concern cannot be dismissed by saying that brokers generally do not claim commissions under such circumstances. Listing brokers often will not make such claims because they hope to continue their relationship with their seller and get another, perhaps larger, commission later on. But cooperating brokers—whose asset is a buyer, not a listing—cannot follow the same strategy; rejection of their buyer’s matching offer gives them no right to a commission from a later sale to a different buyer. They are likely to consider filing suit rather than accepting the loss gracefully.

One of the potential horribles mentioned in RealPro is quite problematic. If the market is surging (as it was in 2005, when RealPro’s offer came in), then multiple offers may be common, and many may be unconditional and match or exceed the asking price. Most standard listing forms do not settle the question of how many commissions can be owed in such circumstances, nor provide any basis for a second cooperating broker to agree that the matching or above-asking-price offer it had procured did not earn it a commission simply because another offer from another broker had been presented first. Obviously the minority rule, with its requirement that a deal close before a commission is earned, eliminates this concern. (The authors are not suggesting that that feature alone is a sufficient reason to prefer the minority rule.) But what about the outcome everywhere else?

The status of cooperating brokers is not always clear, especially with respect to a seller. In California, an authorized subagent has standing to sue an owner directly for her share of a commission. See, e.g., Berry, 228 Cal. Rptr. at 696-97. The listing agreement in RealPro reinforced this concept, explicitly authorizing the cooperating broker to enforce the terms of the listing “against Owner or Agent” (as a third-party beneficiary). RealPro, 138 Cal Rptr. 3d at 256. But not all jurisdictions have similar rules, similar underlying statutes, or similar listing forms. Local MLS rules regarding commission splits also can affect the question; they often provide for
arbitration between the brokers in such cases, but that is little help when the listing broker has received nothing to begin with because the broker tolerated the deal’s failure. The nature of the listing should also affect the result. All open listings are assumed to be automatically terminated when an owner accepts an offer under one listing. See Kennedy & Kennedy v. Vance, 202 P.2d 214 (Okla. 1949); Burke, Law of Real Estate Brokers § 2.02. In any event, the existence of cooperating brokers seems relatively unlikely in open listing situations. But when an exclusive listing is involved and a second offer arrives while the owner is simply mulling over the first offer, double commission liability may be quite uncertain, both for the brokers and the lawyers representing them.

RealPro’s reasoning—as much as its outcome—should warn California brokers that uncritical reliance on the traditional “ready, willing, and able” rule may be an unsuccessful and risky strategy, and that more nuanced and negotiated language should replace their present forms.

Modifying the Listing: A New York Perspective
In New York, where attorneys play a much larger role in all stages of the real estate sale process, it is common for the seller’s counsel to modify brokers’ listing agreements by adding words like, “The commission is payable only as, if, and when title passes, except for willful default on the part of the seller.” Would that solve the RealPro situation of the full-price offer that is rejected?

The situation actually occurred some 28 years ago in Graff v. Billet, 477 N.E.2d 212 (N.Y. 1984), in which the listing agreement contained the language quoted in the paragraph above. The New York Court of Appeals, like the California Court of Appeals, nevertheless denied the broker’s claim for a commission. The court observed that the broker was the party that had inserted the “except for willful default on the part of the seller” language into the listing, which entitled the court to construe it against the broker and hold that refusing to enter into a contract in the first place is not the same as defaulting on a contract after it is formed. There was a stirring dissent by Judge Kaye, arguing that:

permitting the seller unilaterally to defeat the broker’s right to a commission by withholding his signature from a perfectly acceptable contract of sale contravenes the fundamental proposition—rooted in considerations of fairness and justice—that a party cannot take advantage of a failure of a condition precedent caused by his own conduct.

Id. at 215. But the majority opinion was five to two against her.

More recently, 2004 Bowery Partners LLC v. E.G. West 37th LLC, 932 N.Y.S.2d 763 (N.Y. Sup. Ct. 2011) (table, text in Westlaw), also involved a seller that included in the listing agreement the common New York language that “[t]he commission shall be due and payable only as, if, and when title passes.” But after receiving an offer, the seller demanded that the contract of sale contain no conditions, meaning that all due diligence by the buyer would have to be performed before the contract was executed. A buyer procured by the broker was willing to pay the full listing price of $21 million but would not agree to the “no-condition” demand. Subsequent negotiations broke down, no sale contract was signed, and the seller refused to pay the broker’s commission. The New York Supreme Court upheld the seller’s position.
It is certainly unusual for commercial real estate to be sold on a “no conditions” basis, because it forces the buyer to spend a great deal of money on due diligence before the buyer has any assurance of being able to buy the property. But a seller taking that position ought to make that position clear in the original brokerage agreement, and if the broker agrees, the broker will doubtless be bound by it and cannot earn a commission unless procuring a buyer that will agree to that particular form of contract.

If there is no reference in the original brokerage agreement to the acceptable terms of the contract, can the seller add such terms later and thus escape commission liability if the buyer refuses to agree to it? Because a seller can simply refuse to enter into a contract at all (under Graff, supra), then perhaps a fortiori, the seller can erect whatever roadblocks it wishes and similarly avoid the commission if those roadblocks derail the contract negotiations. Yet this seems quite unfair to the broker.

These decisions may be admirable from the viewpoint of protecting sellers, but they can have harsh consequences for brokers. In effect, the courts in New York and California are construing brokerage agreements to commit the broker to work to find a buyer with no assurance at all that the broker will get paid for the effort, even when successful. This result may make more sense in an open listing, in which a broker expects to be paid only if she herself finds a buyer, and may assume that there are other brokers with rival listings working simultaneously. In this situation, rulings that protect a seller from having to pay two commissions when there is only one sale make sense. Perhaps that same risk of double commission liability exists with an exclusive listing when two cooperating brokers produce offers; as indicated above, it is hard to be sure on this point. If so, the courts seem to be working hard indeed to protect sellers against that risk.

Counsel for brokers need to be alert to the potential loss of a commission even when they have found a qualified buyer and, if possible, to address the concern with specific language. It is not hard to draft an agreement under which a commission is definitively earned if the seller is presented with a full price offer and refuses to enter into a contract. But whether brokers will attempt to create such agreements may well depend on market conditions. At least at present, New York brokers rarely try to negotiate such language; perhaps they would rather have the listing, with its accompanying risk that the seller will decide not to sign a sales contract and that the commission will therefore be lost, than not to have the listing at all.

In sum, recent decisions in both California and New York have been very favorable to sellers (and disadvantageous to brokers). The California Court of Appeals in Real-Pro required that a closing occur as a precondition to liability for a commission, even when the parties did not include any such precondition in their listing agreement. Although there is no indication that New York would imply that sort of condition, if the parties have inserted it in the listing, New York courts clearly are willing to read it in a way that is highly beneficial to sellers—allowing the seller to refuse to sign a contract of sale in Graff and allowing the seller to insist on a contract with highly unusual terms in 2004 Bowery Partners.

Other states may not be so pro-seller as New York and California, even when the listing agreement contains language protecting the seller from paying a commission unless there is a
closing. Seventy years ago, Justice Hurst of the Oklahoma Supreme Court took a view similar to that of Justice Kaye’s dissent in Graff:

There are many cases, however, where the contract contained a stipulation that no commission was payable “if the sale for any reason is not consummated” or similar stipulations. By the great weight of authority the courts, in these cases, hold that such contracts do not contemplate an arbitrary refusal to sell on the part of the owner, and that if he does so refuse, or if the sale is prevented by his fault or some arbitrary act on his part, the commission is payable despite the fact that the sale was “not consummated.”

Aetna Lfe Ins. Co. v. Home, 145 P.2d 189, 193 (Okla. 1943) (Hurst, J. dissenting). The effect of Justice Hurst’s comment is much like imposing a duty of good faith and fair dealing on the seller—a duty that exists even when the listing agreement says a commission is due only on closing of the sale. This result is quite different from—indeed opposite to—the New York courts’ positions in Graff and 2004 Bowery Partners.

Conclusion

These cases may be helpful to lawyers in all states, because they provide a useful sampling of the kinds of disputes that can arise between sellers and brokers. With a carefully negotiated listing contract, the variations among the states in their treatment of listing agreements can become largely irrelevant. Sellers obviously need language that will protect them against having to pay a commission if buyers default and fail to close on the sale. But brokers equally need language that will entitle them to commissions when they find qualified buyers that offer full price, but are not able to close because the seller refuses to sign a contract of sale, imposes unreasonable and unexpected conditions in the contract of sale, or simply breaches the contract. A contract clause that accommodates all of these needs should be worth the time and effort of both parties to draft.

A few final thoughts:

1. Always use a written listing agreement. In many states, the Statute of Frauds demands it, but even if not, a written agreement eliminates fights over just what kinds of conditions were agreed on.

2. The wise seller will insist on the condition that “the commission is payable only as, if, and when title passes.” This will eliminate the risk to the seller of owing a commission if the buyer breaches the contract of sale, as well as the risk of owing a double commission if two complying offers are presented by two cooperating brokers.

3. The wise broker will make sure the above language is qualified by “except for willful default on the part of the seller.”

4. The parties should expressly state whether a commission is earned if no closing occurs because the seller declines to accept a full-price offer that conforms to the terms of the listing. If a commission will be owed on these facts, a careful seller will set a high enough listing price so as not to be dissatisfied with a full price offer.
5. If the seller expects to impose unusual terms or conditions in the contract of sale (which might raise a question of whether the seller is acting in good faith), the broker and seller are well advised to expressly agree, in the brokerage agreement, that those terms will be part of the contract of sale.

The end