DEFAULT CLAUSES – ANOTHER EXAMPLE OF POOR DRAFTSMANSHIP

by Harold I. Levine

The default clause in the average real estate contract is poorly drafted. Like the possession clause and the mortgage contingency clause, it needs substantial revision in order to protect the lawyer and his client from serious trouble and possible claims in certain situations.

A typical default is as follows: "If the contract is terminated without purchaser's fault, the earnest money shall be returned to the purchaser, but if the termination is caused by the purchaser's fault, then at the option of the seller and upon notice to the purchaser, the earnest money shall be forfeited to the seller and applied first to the payment of seller's expenses and then to payment of the broker's commission; the balance; if any, is to be retained by the seller as liquidated damages." The default clause in most real estate contracts is totally insufficient to protect the party involved.

If I were representing a buyer and I could change three things in the ordinary real estate contract, my second choice would be to change the default clause. My first choice would be to delete the requirement that the failure to notify the seller of the inability to get a mortgage creates a cash deal (Fund Concept, May-June 1986). As to the third change, keep reading this column to find out.

In any event, if I were representing a seller and I could only change two things, I would modify the default clause to provide as follows:

> It is further expressly agreed between the parties hereto that the remedy of forfeiture herein given to the Seller shall be exclusive of any other remedy.

This is necessary so that the purchaser is not faced with a contract action, specific performance and the like. On the other hand, we have the seller who has title problems and there is concern as to his ability to deliver title. An example may be when the seller is obtaining title through foreclosure, or quiet title action, or in any other circumstances where the seller does not want to be exposed to claims for consequential damages if the deal is not closed. Invariably, the buyer will take the position that the property he was purchasing from the seller was extremely valuable and he was about to lease it to McDonald's and sue the seller for consequential damages, loss of profit and the like. The prudent attorney representing a seller will seek to limit the seller's damages in the contract if the seller cannot deliver title. Below is a sample clause to protect the seller against consequential damages:

> Except as specifically provided herein, if this contract is terminated prior to closing, purchaser shall not be entitled to damages of any type, direct or consequential, it being expressly understood and agreed that the remedies specifically described herein shall constitute purchaser's sole remedies hereunder for seller's default prior to closing, and that purchaser hereby waives any and all remedies not expressly provided herein.

In all cases, there is an obligation on the part of the lawyer to regard the closing as an adversary proceeding, to review the contract, to stop accepting the phrases in the contract without modification or amendment, and above all, to handle real estate transactions promptly. This obligation is an important one to remember, especially in volatile times when the market is behaving erratically.

BURDEN OF ESTATE TAXES ON RESIDUE OF ESTATE

The Fifth District Appellate Court recently held that where a will is silent as to the payment of taxes or other debts, the payment of those debts must first be made from the residue of the estate.

In this case, the court construed a will and codicil with respect to federal and Illinois estate tax payments. The 17th paragraph of the will stated that any bequest or devise made, on which there may be an inheritance due, shall be net to such legatees and devisees, and any such tax due to such legatee or devisee shall be paid out of the residue of the estate. Neither the will nor the codicil in this case expressly referred to estate taxes. Appellant was bequeathed the residue of the estate.

The court used the "burden on the residue" rule which states that where a will is silent as to the payment of taxes or other debts, Illinois case law requires that payment first be made from the residue of the estate. The will in this case was without comment as to estate taxes. The appellants tried to argue that the will showed the testator's intent that estate taxes shouldn't be paid from the same fund as inheritance taxes. Because the will did not indicate that the testator was not aware of the difference between estate taxes and inheritance taxes, the court presumed that the testator used the phrase in its proper sense.

The court interpreted the 17th paragraph of the will to mean that beneficiaries shall be held harmless with respect to payment of the inheritance tax. In conclusion, the court stated that the testator intended matters not mentioned to be handled in customary fashion. Therefore, the appellate court held that the payment of taxes and other debts must be made from the residue of the estate, as is customary.

Haberl v. County of Monroe, 142 Ill.App.3d 152, 96 Ill.Dec. 630, 491 N.E.2d 909 (1986).

ADMISSION AS BASIS FOR SUMMARY JUDGMENT

A recent appellate court decision held that summary judgment was properly granted where, in an affidavit, the president of a condominium's board of managers admitted that no special assessment had been levied against the condominium unit owned by defendants, despite the board's verified complaint in which it was alleged that a special assessment had been levied.

When the defendants contracted to purchase their condominium unit, they asked the board of managers for a written statement for any unpaid assessments owed on the unit. The board notified them that $375 was due. How-