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## Real Estate Contract Unenforceable: Nonrefundable Deposit

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The California Court of Appeal, in Kuish v. Smith (2010 WL 373225), recently held as unenforceable a term in a contract for the purchase of real property which provided for a “nonrefundable” escrow deposit.

Kuish involved a \$620,000 escrow deposit for the purchase of a \$14 million oceanfront home in Laguna Beach. Instead of using a liquidated damages provision, the buyer and sellers merely agreed that the deposit would be “nonrefundable”. According to the trial court, both parties were sophisticated business people who understood the ramifications of their negotiation of non-refundable deposit.

The buyer eventually cancelled the agreement and the sellers refused to refund the buyer’s deposit, even though the property ultimately was sold to a third party for \$1 million more than the contract price the buyer and sellers in Kuish had negotiated.

The buyer in Kuish sued to recover the \$620,000 deposit. Ruling in favor of the buyer, the appellate court stated that “any provision by which money or property would be forfeited without regard to actual damage suffered would be an unenforceable penalty. To construe the term ‘nonrefundable’ to establish [the sellers’] entitlement to the full deposit without regard to actual damages would essentially create a liquidated damages provision.” However, the parties in Kuish did not separately sign or initial a liquidated damages provision.

California real estate brokers and salespersons commonly prepare various standardized real estate purchase contracts, at the direction of their principals. Most real estate brokers and salespersons,

however, are not licensed to practice law and thus should not engage in activities which constitute the practice of law. The unauthorized practice of law, a violation of Business & Professions Code § 6125, generally includes giving “legal advice and counsel and preparation of legal instruments and contracts whereby legal rights are secured, regardless of whether such matters are depending in court.” Agran v. Shapiro, 127 C.A.2d Supp. 807 (1954).

An authoritative encyclopedia of California law, *California Jurisprudence*, states that, “. . . an established business custom sanctions the activities of real estate and insurance agents in drawing certain agreements in business transactions in which they take part in their respective professional capacities.” The editors then quote an article by Robert L. Lancefield which stated: “While these actions are technically within the usual definition of practice of law, they are generally recognized as proper where: [1] the instrument is simple or standardized; [2] the draftsman or intermediary does not charge any fee for such work (other than his regular commission for the transaction); and [3] the drafting is incidental to his other activities in the transaction.” 29 California Law Review 602. Nevertheless, “[s]election and use of a form by the broker may sometimes require a lawyer’s help.” *Reference Book: A Real Estate Guide*, 222-223 (State of California, Department of Real Estate, 2000).

Although it is unclear from the court’s opinion in Kuish whether either or both of the parties in that case were represented by real estate brokers, one might wonder whether they would have regarded advice from real estate brokers concerning whether to initial a \$620,000 liquidated damages clause in a standardized purchase contract to have been

“incidental to [a real estate broker’s] other activities in the transaction” or, on the other hand, whether they might regard such advice to have constituted the unauthorized practice of law.

Earle Law Offices provides trial and appellate litigation, as well as non-litigation, legal services in the areas of business law, constitutional and civil rights law, family law, real estate law, tax law, and trusts and estates.

\* Mr. Earle is licensed to practice law in all California state trial and appellate courts, the United States Supreme Court, the United States Court of Appeals for the Fourth and Ninth Circuits, federal trial courts in the Northern District of California, and the United States Tax Court. He has served as a Judge Pro Tempore for the Santa Clara Superior Court, and is also a licensed Real Estate Broker.

Mr. Earle received his law degree from the Santa Clara University School of Law, where he served as an Editor of the school’s Law Review, and where he received awards for academic excellence. He received his undergraduate degree, with honors, in business administration from the University of La Verne.

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