

# REALTORS® LEGAL ALERT

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## COMMERCIAL BROKERAGE - SUMMARY OF LAWS

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### INTRODUCTION

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The Connecticut Association of REALTORS®, Inc., as part of its outreach to the commercial brokerage community, obtained changes to several state statutes involving commercial real estate. The purpose of these changes was to provide flexibility to the commercial real estate practitioner in dealing with its customers and clients, who are a population of diverse and sophisticated business people. This Legal Alert will summarize the statutory changes that have taken place over the last four years that have an impact on commercial real estate practitioners.

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### DEFINITION

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The very first change was to define what constituted a "commercial real estate transaction." It is impossible to provide separate sets of rules for commercial real estate practitioners unless there is some agreement on what constitutes a "commercial real estate transaction." Accordingly, the Legislature adopted the following definition of a "commercial real estate transaction": *any transaction involving the sale, exchange, lease or sublease of real property other than real property containing any building or structure occupied or intended to be occupied by no more than four families or a single building lot to be used for family or household purposes.* Therefore, industrial buildings, commercial leases, large tracts of open land and other real estate that does not contain a one to four family residence is considered a "commercial real estate transaction. Let us now turn to the separate

rules that apply in commercial real estate transactions.

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### THE COMPENSATION AGREEMENT

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In Connecticut, there are generally only three ways to create an enforceable compensation agreement. When the seller or landlord agrees to pay compensation, the real estate broker will obtain a listing agreement. When the buyer or tenant agrees to be obligated to pay the compensation in which event the real estate broker will obtain a buyer or tenant representation agreement. Broker-to-broker compensation arrangements such as MLS and other co-brokerage arrangements remain unaffected by any of the changes to the statute.

In the case of listing agreements or buyer/tenant representation agreements, however, the statute now provides much more flexibility to the commercial real estate practitioner. In order to create an enforceable compensation agreement with a seller or landlord, the real estate broker will need either a formal listing agreement complying with all of the requirements of Connecticut law or, alternatively, may use a letter, memorandum or other writing provided that the writing meets four very basic requirements. First, the writing must be signed by the party who is going to be responsible for paying the commission. This need not be the record owner of the property. Secondly, the writing must have a duration, i.e. an ending or termination date. Thirdly, the writing must state the amount or the formula to be used to calculate compensation. Finally, there must be a notice that the broker has the right to place a broker lien on the property if the

compensation is not paid. This last requirement may be met by a separate writing. A form for the broker lien notice is available on CAR's website <http://www.ctrealtor.com/forms/>. Buyer/tenant representatives have the same flexibility. In other words, a buyer/tenant representative must either have a buyer/tenant representation agreement containing all of the requirements of Connecticut's statute or, alternatively, may use a writing containing the same requirements discussed above, including notification of broker lien rights.

These changes mean, for example, that so long as a corporate legal department's form listing agreement meets these four basic requirements, it will pass as an enforceable compensation agreement in Connecticut. Similarly, a letter agreement with a buyer or tenant that meets the four basic requirements will serve as the agency agreement needed to show another firm's listing. This provides the commercial real estate practitioner with a great deal of flexibility when dealing with a corporate legal department or potential client who will not sign a formal Connecticut listing or buyer/tenant representation agreement.

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#### WHO SIGNS?

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Most commercial real estate practitioners learned in their Principles and Practices course that all of the record owners of the property must sign a listing agreement for the listing to be valid. The "record owner" requirement was imposed by the courts. The courts imposed this requirement because the original listing law stated that a listing agreement for any real estate had to be signed by the "owner of the real estate." The courts interpreted "owner of the real estate" to mean "record owner" as revealed in the land records.

This caused a hardship in the commercial brokerage community where commercial real estate can be held by a dizzying variety of different entities some of which are single purpose entities that have no assets other than the real estate. For this reason, commercial real estate practitioners were forced to try and obtain personal guarantees or use other measures in order to guarantee commission payment when dealing with entities that had no

assets other than the real estate, and the real estate had little or no equity.

This is another area where more flexibility has been granted to the commercial real estate practitioner. As a result of the change, there is no longer a "record owner" requirement with regard to a commercial real estate transaction. In a commercial real estate transaction, the broker may have the compensation agreement, whether a listing or the informal writing discussed above, signed by the person who will be responsible for paying the compensation *even if this person is not the record owner of the real estate*. While this may seem strange, keep in mind that a real estate listing agreement is essentially an agreement for the purchase of the broker's services, and there is nothing that inherently limits a person's right to engage the services of a real estate broker to attempt to sell real estate that the person does not own.

This is an extremely useful and flexible change in the law because it removes the necessity of having to obtain personal guarantees when dealing with single purpose entities with questionable equity positions. For example, if the real estate broker does not wish to take the listing from the corporation that is the record owner of the real estate because the corporation is a single purpose entity and the equity position of the real estate is not good, the real estate broker can obtain a listing and earn a fee in accordance with the listing from some other person, such as the sole shareholder of the entity. This is also useful where the party wishing to engage the services of a real estate broker holds an option or other right on the property but is not yet the record owner of the property. Prior to this change, the real estate broker would have to pursue a listing agreement from the record owner of the property in order to have an enforceable compensation arrangement even though the record owner may not have any interest in marketing the property. With these changes, the holder of an option can market a property before exercising the option, and the real estate broker can obtain an enforceable compensation arrangement for doing so.

Commercial practitioners are cautioned that if they have their agreement executed by an entity that the

signature be in the proper form. Commercial practitioners should also be aware of the identity of the signatory on their agreement. For example, if the commercial practitioner wants the agreement executed by a partnership, the partnership name should be used in the agreement. Similarly, if the signatory is a corporation or a limited partnership, the name of the corporation or limited partnership should be used. In each of these cases, the signature by the officer or the general partner or the manager should be in the proper format. Sample formats are attached to this Legal Alert.

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### **CORRALLING THE RUNAWAY LANDLORD**

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Another change in the law added a remedy for commercial real estate practitioners to collect renewal commissions on leases. Prior to the change, the only recourse for a commercial real estate practitioner was to place a broker lien on the property. Not only did the broker's lien sometimes serve as a declaration of war, but there were limitations on how and when it could be placed. At the same time, however, the commercial real estate practitioner had to worry that the original signatory on the listing agreement would sell the building, and the new owner would renew the lease with the tenant without acknowledging the broker.

Fortunately, the Legislature provided a new tool in these cases. If the broker files a notice on the land record within thirty (30) days of the date that the lease is signed stating that the broker has a listing agreement providing for renewal commissions, any purchaser of the building will, by law, assume the renewal commission obligation. Although the notice does not constitute a lien on the property, as a practical matter the notice serves to notify any potential purchaser that he or she will be obligated to pay the broker a renewal commission in accordance with the original listing agreement if he or she keeps the tenant. Therefore, a potential purchaser will certainly discuss this with the seller, who was the signatory on the original listing agreement, and the broker can expect to be contacted concerning the notice.

Brokers who are contacted as a result of having filed a notice of renewal commissions, have several choices. They can stand on their original listing

agreement which will be assumed by the new owner and let the buyer and the seller work out how they wish to provide for the commission due in that case. The broker can also reach a settlement with the seller who was the original signatory on the listing agreement. The broker may also reach a replacement agreement with the potential buyer concerning the renewal commission. A form for the notice can be found on CAR's website at <http://www.ctrealtor.com/forms/>.

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### **AGREEMENTS WITH OUT-OF-STATE BROKERS AND SALESPERSONS**

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Public Act 04-83, which takes effect on October 1, 2004, validates cooperative agreements between Connecticut and out-of-state brokerages. Prior to this legislation, the Connecticut Supreme Court had held that it was illegal for both the Connecticut broker and the out-of-state broker to collect compensation when the out-of-state broker performed "core services of real estate brokerage" concerning a Connecticut property. The Public Act legislatively overrules this court case.

The new legislation places some very basic requirements on the agreement between a Connecticut broker and the out-of-state broker. Essentially, the terms of the cooperative effort between the two brokerages must be in a written agreement specifying any compensation to be paid by the Connecticut broker to the out-of-state broker. The agreement must also contain a statement that the out-of-state broker and the out-of-state broker's agents will comply with the laws of the State of Connecticut. In addition, the Connecticut broker must obtain a copy of the out-of-state broker's license or other proof of licensure from the jurisdiction where the out-of-state broker maintains a license as a real estate broker. Finally, any escrow funds, security deposits, or other monies received by either of the brokers must be held in accordance with Connecticut law. Similar rules apply to out-of-state salespeople.

Once the agreement is in place, the out-of-state broker may perform any act concerning a commercial real estate transaction that could be performed by a Connecticut real estate broker except showing property in Connecticut. Finally, an

out-of-state broker or out-of-state salesperson advertising Connecticut real estate must include in any advertising material the name of the Connecticut broker with whom the out-of-state broker is cooperating.

requirements of Public Act 04-83 in order to ensure that any commission claim resulting from co-brokerage arrangement is enforceable in Connecticut.

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#### ADVICE FOR REALTORS®

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1. Commercial real estate practitioners should keep in mind that a written agreement is always required in order to enforce a commission obligation, but that commercial real estate practitioners have a great deal of flexibility in the type of written agreement that they obtain. Any written compensation agreement that is not a Connecticut form listing agreement should at least contain the minimum requirements outlined above.
2. Commercial real estate practitioners should select the person signing their listing agreement or buyer representation agreement with care. Commercial real estate practitioners generally deal with a variety of entities ranging from corporations to limited liability companies to limited liability partnerships to general partnerships. Since commercial real estate practitioners may enforce their listing and buyer representation agreements against the party who signs the agreement, there is an opportunity to obtain enforceable agreements from parties other than a record owner of the property if to do so would be advantageous to the broker. However, commercial real estate practitioners should ensure that they use the proper format in obtaining signatures from entities.
3. Commercial real estate practitioners who are potentially owed renewal commissions are foolish not to use the new tool to notify potential purchasers that there is a renewal commission if the purchaser renews with the same tenant. For a very nominal recording fee, the new notice is cheap insurance against a "runaway landlord."
4. Ensure that any co-brokerage agreement with an out-of-state broker complies with the

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#### CONCLUSION

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The Connecticut Association of REALTORS®, Inc. has done much in order to assist the commercial real estate practitioner. Commercial real estate practitioners have flexibility in making compensation agreements, choosing parties to execute their written agreements, and collecting commissions on lease renewals. Commercial real estate practitioners should be familiar with the areas where they have such flexibility so they can take advantage of this new flexibility in their practices.

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**THIS LEGAL ALERT FOR REALTORS® IS INTENDED FOR GENERAL INFORMATION PURPOSES AND IS NOT INTENDED TO PROVIDE LEGAL ADVICE ON ANY SPECIFIC FACTS. IF YOU HAVE SPECIFIC QUESTIONS CONCERNING YOUR OWN SITUATION, PLEASE CONSULT YOUR ATTORNEY.**

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**SIGNATURE FORMATS FOR ENTITIES**

**CORPORATION**

XYZ, Inc.

By \_\_\_\_\_

Its [Title of the Officer Signing]

**PARTNERSHIP**

XYZ, a General Partnership

By \_\_\_\_\_

Its Partner

**LLC**

XYZ, LLC

By \_\_\_\_\_

Its [Manager, if LLC has a manger] or [member]

**LIMITED PARTNERSHIP**

XYZ, Ltd. Partnership

By \_\_\_\_\_

Its General Partner