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GAZUMPING—NOW THAT IT MATTERS AGAIN

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Introduction

Ever since gazumping raised its head in the wake of the extraordinarily volatile market in land which developed in England (and Ireland) in the 1970s, it has so far managed to remain a major, albeit unwelcome, feature of the property market. The new Labour Government has, on assumption of office in May 1997, issued a Consultation Paper, titled *No to Gazumping*, by which it invited comments on the problems caused by and ways to tackle the practice of gazumping. The Government is now studying the different proposals meant to arrest the problem, but certainly, the difficulty of the topic necessarily means that it would take some time before the Government comes up with a solution. However, it is not clear if or how far the Government would succeed in its search for a solution. This paper examines the reasons for the practice of gazumping and proffers suggestions on how to curb it.

Meaning of gazumping

The word "gazump", or variants of it,[1] is generally taken to mean "to swindle or give short change" or act improperly.[2] As it has come to be used in relation to the purchase of a house, "gazumping" describes the situation in which the seller of a house accepts or threatens to accept a second purchase offer, having already accepted a prior (but lower) offer from another buyer. In other words, the seller changes or threatens to change his allegiance to a second buyer who offers more money. It is generally decried as unconscionable and unprincipled that the first buyer should be bypassed in this circumstance. This is why Keane J. described gazumping as "a practice as unattractive as its name".[3] In his view, once a seller has "shaken hands on a deal", he should not subsequently fall for the temptation of a (substantially) more attractive offer.[4]

The practice of gazumping

In England, the practice of gazumping is the scourge of the residential property market. Once house prices hit the roof, buyers begin to panic that they may find their potential dream home rising in value out of their "price range". Sellers, on their part, look out for higher and higher offers. Presently, the housing market is at a high and the practice of gazumping is so widespread that it earned for itself a place in a popular soap opera, the television's *EastEnders*.[5] As the demand for house purchase outstrips supply,[6] the National Association of Estate Agents reports that in London alone, gazumping affects 1 in 10 transactions,[7] and affects 1 in 20 transactions nationwide.[8]

It is easy to accuse the seller of gazumping, but it would, perhaps, be worthwhile to also consider the reason(s) why he gazumps. The practice of gazumping is borne out of financial prudence, and it is done with, at least, the passive acquiescence of the law. All criticisms of the practice are mainly on moral grounds: its "unfairness to the

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[3] *Mulhall v. Harren* [1981] I.R. 364 at 378.

[4] *ibid.*

[5] "How to stall the gazumpers", *News of the World*, August 3, 1997, p. 42.

[6] See, *e.g.* "Housing shortage drives up prices" *The Mirror*, May 23, 1998, p. 2 ("Home Life" pullout).

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GAZUMPING—NOW THAT IT MATTERS AGAIN

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buyer". As a prudent man of business, which the seller is, the law as it stands does not expect or require him to accept a lower offer in preference to a higher one even if the lower offer was the first in time. This is due to the development of the notion of making agreements "subject to contract". It is generally known, as a basic rule in the law of contract, that an agreement which is made "subject to contract" is not legally binding until and unless a formal contract is drawn up and exchanged.[9] There is thus nothing illegal where the seller who has agreed, subject to contract, to sell a property to B, afterwards sells it to C.[10] Indeed, since the law does not prohibit the practice, it may be said that the law permits it and that is why gazumping persists till today. There may be no direct authority for this view, but a duty to gazump has been held to exist in the case of trustees who, being in some fiduciary position, are bound to sell at the best price reasonably obtainable. Wynn-Parry J. made it clear, in *Buttle v. Saunders*,[11] that if trustees for sale having agreed to sell "subject to contract" to A for £x, then receive a "serious" offer from B to pay £x + y, then subject to there being no disadvantage in accepting B's offer such as would outweigh the prima facie advantage of the higher price, the trustees would commit a breach of their duty to obtain the best price, if they were to sell to A for £x rather than to B for £x + y.[12]

There is no gainsaying that gazumping often inflicts great detriment on the buyer,[13] but that is not to say that the buyer is never to blame for the occurrence of gazumping; the buyer may be the one who, by his indecision or other attitude, compels the seller to gazump. Imagine, for instance, a seller who put up his property for sale at £200,000 and a buyer offers, say, £195,000 subject to survey. The buyer haggles about the fixtures and fittings to be included and eventually, just before the exchange of contracts, requests that in view of his expenses, the seller should make a further reduction. This would cause the seller to "gazunder" the buyer in preference for a higher (or better) offer. Or, take another instance, where the buyer, after making a "subject to contract" offer, discovers that he is unable to raise enough loan to finance the purchase; or where he simply changes his mind; or where he never really intended to pay the sum he offered but merely meant to use the "subject to contract" offer to induce the seller to keep the property off the market so as not to get higher offers. These are not mere imaginary scenarios. Indeed, as far back as in 1973, the Law Commission had found, based on the information of an estate agent with an extensive practice handling the sale of "second hand" houses in outer London and the suburbs, that it is not only the seller who breaks a "subject to contract" agreement. In the words of the Commission, "many more bargains were failing to result in contracts through withdrawals by buyers than withdrawals by sellers".[14] Sadly, however, unlike the seller who is said to "gazump", there is no equally "unattractive" term to describe the action of the buyer who pulls out of a "subject to contract" house sale agreement so as to buy a cheaper (or better) one.

It is submitted that even where the buyer suffers a detriment as a result of the seller's act of gazumping, such as where the buyer has expended money on solicitor's fees, survey and search fees, such detriment should be seen as a voluntary assumption of risk for which the "gazundered" buyer cannot complain.[15] As emphasized in *Regalian Properties plc v. London Dockland Development Corp.*,[16] where parties enter into negotiations with the intention of concluding a contract but on the express terms that each party is free to withdraw from the negotiations at any time (such as by the deliberate use of the words "subject to contract", with the admitted intention that they should have their usual effect), it is clear that, pending the conclusion of a binding contract, any loss incurred by one of the parties in preparation for the intended contract would be incurred at his own risk in the sense that he would have no recompense for the loss if no contract results.[17] In other words, the loss, in such case, would "lie where it fell".[18]

It appears that the only instance when gazumping could properly be regarded as unprincipled

[9] *Winn v. Bull* (1877) 7 Ch.D. 29 at 32, *per* Jessel M.R.

[10] In *Gooding v. Frazer* [1967] 1 W.L.R. 286 at 293, Sachs J. spoke of an agreement "subject to contract" as a "transaction which is often referred to as a gentleman's agreement but which experience shows is only too often a transaction in which each side hopes the other will act like a gentleman and neither intends so to act if it is against his material interests". Also, in Jones, G., *Goff and Jones on Restitution* (4th ed., Sweet & Maxwell, London, 1993), it is said that "a gentleman's agreement to pay for services does not bind any gentleman".

[11] [1950] 2 All E.R. 193.

[12] *ibid.* at 195; Scammell, E.H. (1979) Conv. 451.

[13] Such as disappointment and the loss of expectation of acquiring the house. As to the buyer's financial costs (*e.g.* search fees, survey and solicitor's charges), see below.

[14] The Law Commission Working Paper No. 51, *Transfer of Land: "Subject to Contract" Agreements*, July 3, 1973, para. 4.

[15] By analogy with *volenti non fit injuria* in tort cases. See also the next footnote.

[16] [1995] 1 All E.R. 1005.

[17] *ibid.* at 1024.

[18] *ibid.*

(and even so, on the part of the buyer, not the seller), is where the eventual buyer is the gazundered buyer's estate agent or somebody in some other fiduciary relationship with the buyer, so that the purchase is in breach of his duty to the buyer. In a case reported recently in the newspapers,[19] the buyers had submitted, through their estate agent, an offer meeting the full asking price of £81,995 to the vendor. To their dismay, the agent told them that the vendor wanted to wait a few weeks in order to test the market. Unknown to the buyers, the agent then topped just £5 on the offer of the buyers and thus got the property sold to him personally rather than to or on behalf of his clients (the buyers).

One may be tempted to wonder why the vendor should have wanted to still "test the market" even when his asking price has been fully met. This, however, is beside the point, for the vendor is not acting unlawfully in further testing the market in the circumstance, or in gazundering the buyers, so long as gazumping is not illegal. The iniquity here lies with the estate agent who has breached his duties as an agent. It is frequently buyers in fiduciary positions such as this who give gazumping a bad name by using selfishly the information they obtain professionally from their clients against the very same clients.

Though the practice of gazumping is rooted solely in financial considerations, *i.e.* the maximisation of profit, its emergence and continued existence is, as has already been shown above, facilitated by law. It would therefore be proper to turn to the law in the search for ways of curtailing the practice or lessening the hardship occasioned thereby.[20]

The solution

An attempt to find a legal solution to the problem of gazumping appears to have been made for the first time in 1971, when Kevin McNamara M.P. introduced a private member's Bill, titled The Abolition of Gazumping And Kindred Practices Bill.[21] The Bill proposed, *inter alia*, that where a seller had agreed, whether subject to contract or otherwise, to sell a house to a particular buyer at a particular price, it would be a criminal offence for the seller to increase the price or to sell it to any other buyer (at a higher price) unless he paid all the fees and expenses of the disappointed buyer.[22] The Bill could not secure a second reading, but it however prompted a reference of the matter to the Law Commission. The Commission refused to recommend an abolition of gazumping. As regards the proposal for criminalisation, the Commission reasoned, quite rightly, that it would be "unfair to invoke the criminal law against a seller who goes back on his word to obtain more money while leaving the buyer free to resile in order to pay less";[23] and that it would be unjustified to create a new criminal offence in this area which has hitherto been predominantly the province of the civil law.[24]

It may be said that the only legal contribution, and yet a very vital impetus, to gazumping is given by the operation of the "subject to contract" clause in the sale/purchase agreement. The seller may be offered a higher price by the eventual buyer than did the first buyer, but if the seller had entered into a legally enforceable contract with the first buyer, not one which is subject to contract, he would be obliged by law to still sell to the first buyer albeit at a lower price. Indeed, he would not even be looking for further offers as the property would be removed from the market. Sympathy for this view has prompted a call for the abolition of the use of the "subject to contract" clause in respect of house sales, and that instead, the Scottish practice, which is more akin to a sale by tender, be adopted. Suffice it to say that this approach was considered and rightly rejected by the Law Commission.[25]

It should be said that there is no special hardship caused by the operation of the "subject to contract" clause with regard to house sales, which is above

[19] See, for example: "The £5 gazumper" *Daily Mail*, April 17, 1998, p. 3.

[20] Non-legal solutions have been suggested. These include: the buyer having all the relevant documents, *e.g.* his pay slips, ready so as to speed up mortgage application; making a sensible first offer which is close to the asking price, so that the seller would be less likely to seek higher offers. This may, however, not work in all cases because, as has been shown above, even where the buyer offers the full asking price, the seller may still be minded to still "test the market" and a difference of as little as £5 can see him gazumping.

[21] Law Commission Working Paper No. 51, *op. cit.*, para. 54.

[22] *ibid.*

[23] *ibid.*, para. 56.

[24] *ibid.*, para. 59.

[25] *ibid.*, paras 32–40. Other proposals considered and rejected are: binding options to purchase within a stated time (paras 25–28); auction and tender (paras 29–31); conditional contract option (paras 41–51). At the request of the Lord Chancellor, the Council of the Law Society also considered this last proposal but rejected it for the reason, *inter alia*, that "an agreement of this nature, even if rescinded or not proceeded with, might give rise to a claim by a vendor's estate agent for commission". See the memorandum of the Council of The Law Society, dated May 1964.

and beyond that caused in other types of transactions, so as to necessitate a partial abolition of the clause in relation to house sales alone. In any case, the insertion of the clause in a house sale agreement has its great advantages not only to the seller but also to the buyer,[26] and these advantages would be painfully lost if the use of the clause is abolished. This is a point quite often overlooked. One is therefore minded to take the view that although the "subject to contract" clause is the legal basis of the gazumping practice, there is no special reason for abolishing it in relation to house sales alone. Indeed, there are, on the other hand, strong reasons for retaining the clause: both parties are aware of, professionally advised about, and voluntarily agree to its insertion in the agreement to their mutual benefit. It is of course probable that abolishing the clause would put an end to gazumping, as there would be no interval between agreement of price "subject to contract" and exchange of contracts. However, there is, on the other hand, an equal probability that such "closure of the interval" would have its own attendant difficulties which may, in the long run, be greater than those attendant on gazumping.[27] As it is, it would appear that even if one borrows the wisdom of Solomon, it may not be possible find a way of legislating against the practice of gazumping without doing more harm than good.[28] The most that can be done is to take steps to minimise its occurrence and mitigate its detrimental side effects on the parties.

Recently, different proposals have been proffered, apparently in response to the new Labour Government's request for comments on the problems caused by the practice of gazumping and the ways to tackle it. The Royal Institute of Chartered Surveyors and JUSTICE have jointly drawn up a form of anti-gazumping and gazundering agreement, with the purpose of deterring the parties to a sale of a property from seeking to re-negotiate the price agreed between them, "subject to contract". The form is designed to apply for a fixed duration and to bind the parties to pay compensation if they withdraw from the agreement or seek to re-negotiate the price, unless one of three defined circumstances applies. These relate to problems with title, the result of a survey and damage to the property. The compensation payable would be based on a percentage of the sale price.

This is a commendable proposal because, first, it is not one-sided,[29] and secondly, it would punish either the buyer or the seller if they pull out of the deal. Sellers would compensate buyers for money spent on surveys, legal fees and fixing mortgages. Buyers would be liable for costs sellers had incurred. Such "cost guarantee" arrangement would not affect the efficacy of the "subject to contract" provision,[30] nor would it eliminate gazumping, but would reduce gazumping by putting a price on it. Such price, it is submitted, has to be reasonably substantial in order to be effective in deterring gazumping.

So far, this proposal is the most well-received by the general public.[31] While it is not unthinkable that a seller who gazumps will ensure that he sells at a price that would cover his deposit for the buyer's loss and still leave him with a substantial surplus, it is our view that occasions may not be frequent when he can get such high second offers even in a typical "seller's market", unless the first offer was ridiculously low. While gazumping cannot be eliminated by a total change in the law, it can be significantly reduced by the adoption of the cost guarantee proposal.

[26] It allows the seller, and the buyer, as the case may be, time to synchronise sales and purchases, arrange mortgage finance, conduct searches and proper enquiries, get legal or other professional advice, etc.

[27] For instance, this would not allow time for enquiries and searches; any defects would be discovered after a binding contract has been concluded.

[28] See also Thompson, M.P., "The fight against gazumping" *Amicus Curiae*, Issue 2 November 1997, pp. 28–29.

[29] This is unlike "lock-out" agreements, in which case, once an offer is made, the seller is "locked out" of considering other bids and can be sued for breaking the deal. This is unfairly biased towards the buyers, because it only "locks out" the seller, leaving the buyer free to withdraw, and if the buyer withdraws it could be hard to prove that they did not have reasonable excuse to do so.

[30] While it would not affect the efficacy of the provisions, in the sense that the parties are still free to withdraw at any time before the exchange of contracts, it would however affect the effect of the provisions, in the sense that the loss would no longer "lie where it fell". It is worth mentioning that despite the strong language used in the *Regalian* case, the court did hint ([1995] 1 All E.R. 1005 at 1020 of the report) that the loss may not always "lie where it fell". That is to say, in some cases the gazundered party (or the victim of a pull out) could, in appropriate cases, be entitled to a recompense, *e.g.* where one party "unilaterally [decided] to abandon the project".

[31] See, *e.g.* "How Labour will trump gazumping" *Daily Mail*, January 23, 1997, p. 13; "Gazumping set for new attack" *Birmingham Metronews: Property News*, May 22, 1997, p. 1.