

NOT AS UNCONSCIONABLE AS SOME MIGHT THINK: COURT OF APPEAL ORDERS PURCHASER TO FORFEIT DEPOSIT AFTER FAILING TO CLOSE REAL ESTATE DEAL

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Vendors and purchasers in real estate transactions should not assume that, just because a deposit is high, a court will grant relief from forfeiture, even if the vendor suffers no actual damages as a result of the purchaser's failure to close the transaction.

In *Redstone Enterprises Ltd. v. Simple Technology Inc.*^[1], the Ontario Court of Appeal overturned a decision granting partial relief from forfeiture of a purchaser's deposit after the purchaser failed to close a real estate transaction.

In allowing the appeal, the Court of Appeal set out factors to consider when determining whether it would be unconscionable to require a purchaser to forfeit its deposit.

The Facts

The real estate deal in question involved the purchase of a warehouse in Brantford, Ontario for \$10,225,000. The purchaser planned to use the warehouse to start a marijuana grow-op business. In order to do so, the purchaser required financing and a license from Health Canada.

In addition to the initial deposits of \$300,000 required under the Agreement of Purchase and Sale (the "APS"), the purchaser paid a further deposit of \$450,000 to secure an extension of the closing date when the Health Canada license took longer than expected.

Ultimately, the purchaser could not get the necessary financing or Health Canada license and failed to close the transaction. When the purchaser refused to agree to a release of the deposits, being held in trust by a third party, the vendor brought an application for a declaration that it was entitled to be paid the deposits.

The Trial Court's Decision

Under section 98 of the Courts of Justice Act,^[2] the court has discretion to grant relief against penalties and forfeitures, on such terms as to compensation or otherwise as are considered just.

In order to obtain relief from forfeiture, the purchaser must meet a two-part test:

1. the proposed forfeited sum must be out of proportion to the damages suffered by the vendor; and
2. it would be unconscionable for the vendor to retain the deposit paid.^[3]

With respect to the first part of the test, the trial judge found that there was no evidence before the court as to whether the vendor suffered any damages. Accordingly, it was impossible to determine whether \$750,000 in deposits was proportional to the damages suffered, or not.

With respect to the second part of the test, the trial judge concluded that \$750,000 in deposits “reaches a level where complete forfeiture becomes unconscionable, in the absence of any evidence concerning damages suffered by the vendor.”^[4]

The trial judge accordingly granted partial relief from forfeiture, ordering that only \$350,000 of the purchaser’s total deposit be forfeited to the vendor.

The Appeal

The Court of Appeal found that a lack of evidence of any damages suffered by the vendor did not render forfeiture of the deposits unconscionable. While in some circumstances, a disproportionately large deposit could be unconscionable, that was not the case here.

The Court of Appeal noted that deposits paid pursuant to a contract for the sale of land are an exception to the general rule that an amount subject to forfeiture resulting from a breach of contract is unlawful, unless that amount represents a pre-estimate of damages suffered. Accordingly, a deposit may be forfeited, even if the deposit amount has no reference to the vendor’s anticipated damages.

In cases where there is no evidence of gross disproportionality in the size of the deposit, as here, the court must consider the full commercial context when assessing whether the forfeiture of a deposit is unconscionable. In this case, the Court of Appeal considered the following factors:

- the parties did not have an inequality of bargaining power;
- both parties were sophisticated;
- the parties engaged in *bona fide* negotiation;
- there was no fiduciary relationship between the parties;
- as the closing date approached, the purchaser raised spurious complaints in an effort to escape from the transaction, while the vendor remained ready and willing to close and was prepared to extend the closing date without additional payment; and
- the total deposit was slightly more than seven per cent of the purchase price, which was not an unfair

range.

A finding of unconscionability will only be made in exceptional circumstances. After considering the above factors, the Court of Appeal concluded that there was no unconscionability in this case. While the vendor may have driven a hard bargain with respect to its request for deposits, this circumstance does not constitute unconscionability.

by Jason J. Annibale and Cara Zacks

[1] 2017 ONCA 282 (“*Redstone*”).[ps2id id='1' target=""]

[2] R.S.O. 1990, c. C.43.[ps2id id='2' target=""]

[3] *Varajao v. Azish*, 2015 ONCA 218.[ps2id id='3' target=""]

[4] *Redstone*, para. 10.[ps2id id='4' target=""]

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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