thestar.com

Bob Aaron bob@aaron.ca

**December 9, 2006**

# Buyer beware when it comes to deposits

What happens when you sign an agreement to buy a house from a builder but later change your mind?

That was the question an Ontario court had to deal with in a case heard earlier this year. On Sept. 15, 2003, Shanker Iyer and his mother Bala Ramachandran signed an agreement to buy a new home for $280,900 from Pleasant Developments.

The offer was accepted by the builder on Sept. 16, 2003. The following day the buyers attempted to cancel the agreement verbally, and a few days later their lawyer advised the builder in writing that the buyers considered the deal dead and wanted the return of their $10,000 deposit.

Iyer believed the document he signed in the sales office was "only an offer" and said he was told by the sales person that he had 10 days to change his mind and cancel the deal.

He also stated that he asked for a copy of the agreement but did not get one.

The transaction never closed and the buyers sued the builder for return of their deposit.

In July 2005, the matter came up for trial in the Richmond Hill Small Claims Court. The trial judge found that there was no coercion or misrepresentation in the sales office. He ruled that the buyers had no justification for cancelling the contract and that they were in breach by refusing to complete the transaction.

The important question, however, was whether the buyers would have to forfeit their $10,000 deposit when the builder did not suffer or prove any damages as a result of the breach.

Ontario courts have the power to make orders relieving a party from forfeiture of a deposit in appropriate cases.

In this case, the trial judge ruled that if the builder was allowed to keep the deposit, it would be "grossly disproportionate" to the losses suffered by the builder which the judge decided were minimal.

In order to prevent the builder from gaining a "windfall," the judge exercised his discretion and ordered the builder to return $9,300.

It was allowed to retain a nominal $700 for legal fees and other damages.

Not satisfied with the Small Claims Court decision, Theodore Rotenberg, lawyer for Pleasant Developments, appealed the ruling to the Divisional Court. One issue on appeal was whether the builder had to prove damages in order to keep the $10,000 deposit.

On this point, the Divisional Court allowed the appeal by the builder. Justice Michael Brown said that the law is clear that a deposit may be forfeited without proof of damages even where the seller resells at a profit.

In law, a deposit is an "earnest" or "guaranty" to bind the purchaser to the transaction. Simply stated, it gets forfeited if the purchaser defaults.

The other question for the Divisional Court was whether the purchasers were entitled to relief from the seizure of their deposit.

Under Ontario law, there are some circumstances where the loss of a deposit may be subject to relief from forfeiture. The court has the inherent power to return a deposit to a defaulting purchaser:

- If it regards the seizure as a penalty
- If the deposit is out of all proportion to the losses suffered by the seller
- Where it would be unconscionable to allow the seller to keep the money

In this case, Justice Brown ruled that the deposit was only 3.6 per cent of the purchase price. It was not out of proportion to the builder's losses and it was not unconscionable to allow the builder to retain the deposit.

For homebuyers, there are several important lessons to be learned from the case of Pleasant Developments and Iyer:

- Buyer's remorse can be very expensive. Make sure you want the house before you sign on the dotted line.
- Unless the contract has a specific condition to allow for financing or lawyer approval, there is no 10-day cooling-off period for new homes. Only builder offers for new condominiums have a 10-day cancellation period by law.
- A defaulting buyer is responsible for all of the seller's losses, not just the deposit. If the buyer backs out and the builder loses money because the market softens, the defaulting buyer is on the hook for the price difference, carrying costs, legal fees and a host of other losses.
- Promises made by a sales person are not part of the deal if they're not written into the contract.
- Never walk out of a builder's sales office without a copy of the documents that were signed.
- And most important: Always have your offer reviewed by a real estate lawyer *before* signing the contract or before it becomes unconditional.

***Bob Aaron** is a Toronto real estate lawyer. He can be reached by email at bob@aaron.ca, phone 416-364-9366 or fax 416-364-3818. Visit the column archives at http://aaron.ca/starindex.htm.*

==========

**This document: 2006 CanLII 10223 (ON S.C.D.C.)**
**Citation:** *Pleasant Developments Inc. v. Iyer*, 2006 CanLII 10223 (ON S.C.D.C.)
**Date:** *2006-04-05*
**Docket:** *76708/05*

**COURT FILE NO.:** 76708/05

**DATE:** 2006/04/05

**ONTARIO**

# SUPERIOR COURT OF JUSTICE

**DIVISIONAL COURT**

| | | |
|---|---|---|
| **B E T W E EN:** | ) | |
| | ) | |
| **PLEASANT DEVELOPMENTS INC.** | )<br>)<br>) | Theodore Rotenberg, for the Appellant |
| | ) | |
| Appellant (Defendant) | ) | |
| | ) | |
| **- and -** | ) | |
| | ) | |
| | ) | |
| **SHANKAR IYER and**<br>**BALA RAMACHANDRAN** | )<br>)<br>) | Shankar Iyer and Bala Ramachandran, Self-Represented |
| | ) | |
| Respondents (Plaintiffs) | )<br>) | |
| | ) | |
| | ) | **HEARD:** March 14, 2006 |

**REASONS FOR JUDGMENT**

**BROWN J.**

**I BACKGROUND**

[1] This is an appeal by Pleasant Developments Inc. ( the Appellant ) from the judgment of Deputy Judge Kilian of the Small Claims Court awarding the Respondents a refund of $9,300 of a deposit of $10,000 that the Respondents had paid to the Appellant with respect to the purchase of a new home.

[2] The Respondents as purchasers had signed an Agreement of Purchase and Sale with the Appellant as vendor to purchase a new home for $280,900 with a closing date of January 23, 2004. The Respondents paid a deposit of $10,000 to the Appellant who was the developer of the property in question.

[3] The trial judge found that the Agreement of Purchase and Sale was signed by the Respondents on September 15, 2003, and signed by the Appellant the next day on September 16, 2003. On the following day, September 17, 2003, the Respondents attempted to verbally cancel the Agreement of Purchase and Sale. This was followed up shortly thereafter with a letter from the Respondents lawyer indicating that they considered the Agreement of Purchase and Sale at an end and requesting the return of the deposit.

[4] The trial judge found that the deposit should be returned to the Respondents and after deducting an amount of $700 as damages for the Appellant, the trial judge ordered the Appellant to pay the Respondents $9,300 plus interest and costs. The Appellant appeals from this result.

**II ANALYSIS**

[5] The Appellant has raised a number of grounds of appeal from the decision of the trial judge but it is only necessary for me to deal with two issues. Specifically:

1) Was it necessary for the Appellant to prove damages in order to forfeit the Respondents deposit? and

2) Were the Respondents entitled to relief against forfeiture?

I will deal with each of these issues separately.

**(i) Was it necessary for the Appellant to prove damages in order to forfeit the Respondents deposit?**

[6] The trial judge found that the wording of the Agreement of Purchase and Sale was insufficient in the circumstances of this case to forfeit the Respondents deposit without proof of the Appellant s damages. In my view, the trial judge erred in coming to such a conclusion.

[7] The law is clear that a deposit may be forfeited without proof of damages. See *DePalma v. Runnymede Iron & Steel Co*. [1950] 1 D.L.R 557. In other words even in the case where the vendor resells at a purchase price that is high enough to compensate for any loss from the first sale, the vendor may nevertheless retain the deposit. See *Perell and Engell, Remedies and the Sale of Land, 2nd ed* at p. 186.

[8] While I accept that the language of the contract is not by itself determinative, the use of the word deposit will imply that the payment is intended for forfeiture upon the purchaser s breach. See *Perell and Engell, supra*, at p. 187. The common law position is that if the agreement is silent and the purchaser defaults, the deposit, by it very nature is forfeited to the vendor. See *Salavatore et al, Agreement of Purchase and Sale (Toronto: Butterworths, 1996)* at p. 61.

[9] In my view, there can be little doubt that the $10,000 paid by the Respondents in respect of the Agreement of Purchase and Sale was a deposit. The Agreement refers to the money as a deposit. There is nothing in the Agreement to suggest that the deposit is to be returned to the Respondents upon default. Unless an agreement indicates an intention that the deposit is not to be forfeited, the vendor has an implied right to retain it. The Agreement of Purchase and Sale was not completed by reason of the Respondents default and in such circumstances a true deposit is lost. See *Morris v. Cam-Nest Developments Ltd.* (1988), 64 O.R. (2d) 475 (Ont. H.C.J. ) at p. 491.

[10] Based on all the circumstances, I am satisfied that the $10,000 paid by the Respondents was intended to be a deposit in the strict sense of an earnest or guaranty to bind the purchaser to the transaction. In my view, the deposit was forfeited upon the default of the Respondents. In these circumstances it was not necessary for the Appellant to prove damages in order to forfeit the Respondents deposit and the trial judge erred in so concluding.

**(ii) Were the Respondents entitled to relief against forfeiture?**

[11] The trial judge found that relief from forfeiture of the deposit was available to the Respondents in the circumstances of this case. The trial judge found the reason the Appellant proved no damages was because there were no losses or very minimal ones and keeping the deposit would result in a $10,000 windfall for the vendor.

[12] I accept that there are circumstances where the loss of a deposit may be subject to relief from forfeiture. If there is relief, the deposit is returnable, in whole or in part, to the defaulting purchaser. If the Court regards the forfeiture of the deposit as a penalty, then regardless of the wording of the contract, the Court retains the power to relieve the penalty. See *Perell v. Engell, supra*, at p. 187.

[13] The Courts will award relief from forfeiture of the purchaser s deposit only where it is established that the sum is out of all proportion to the losses suffered and that it would be unconscionable for the vendor to retain the money. See *Stockloser v. Johnson*, [1954] 1 Q.B. 476. Where these requirements are not made out, the Courts will allow the forfeiture of the deposit without an inquiry into the extent of the vendor s damages. See *Craig v. Mohawk Metal Ltd.* (1975), 61 D.L.R. (3d) 588 (Ont. H.C.J.).

[14] The onus is on the party seeking to invalidate a clause to show that it inflicts a penalty, rather than determines the damages payable by the guilty party. But even where a clause does inflict a penalty, it will not always be unenforceable where, for example, it is not unconscionable. See *Fridman, The Law of Contracts in Canada, 4th ed. (Toronto: Carswell, 1999)* at p. 817.

[15] I am of the view that the trial judge erred in awarding the Respondents relief from forfeiture of the deposit. In my view, there was not a sufficient evidentiary basis to suggest, as the trial judge did, that the reason the Appellant proved no damages was because there were no losses or very minimal ones and keeping the deposit would result in a $10,000 windfall for the Appellant. As I have indicated previously in these reasons, it was not necessary for the Appellant to prove damages in order to forfeit the Respondents deposit. Accordingly, it was an error for the trial judge to infer that the failure of the Appellant to prove damages was evidence of a windfall for the Appellant.

[16] The onus was on the Respondents to prove that the sum of the deposit is out of all proportion to the losses suffered and that it would be unconscionable for the Appellant to retain the deposit. In my view, on the facts in this case, it was an error to conclude that the Respondents had met that onus. At the date of the Agreement of Purchase and Sale the Respondents were required to pay a deposit of $10,000 towards a purchase price of $280,900 or 3.6% of the purchase price. In all the circumstances, I am not satisfied there was a sufficient evidentiary basis for the trial judge to have concluded that the Respondents deposit is out of all proportion to the losses suffered and that it would be unconscionable for the Appellant to retain the deposit. Accordingly, I am of the view the trial judge erred in finding that relief from forfeiture of the deposit was available to the Respondents in the circumstances of this case.

**III CONCLUSION**

[17] For the above reasons I would allow the appeal of the Appellant, set aside the judgment of Deputy Judge Kilian and substitute a judgment dismissing the Respondents claim. In the circumstances of this case I would order that each party assume their own costs of the trial and this appeal.

Justice M. Brown

**Released:** April 5, 2006