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A Legal Newsletter for the Mortgage and Real Estate Industries

Closing Date Deemed Not an “Essential Term” of Sale Agreement

In an interesting recent case, the court concluded that the closing date was not an “essential term” in an agreement by a land developer to sell 48 vacant lots to a prospective home-builder. The court also ruled that the parties had agreed to amend the closing date, even though a written amending agreement was never signed.

The Agreement of Purchase and Sale between the seller and buyer contained a provision stipulating a year-long range for the closing date, namely within 12 months following the seller’s completion of permit-servicing requirements for the lots, but no later than November 1, 2018. This meant the permits servicing requirements would have to be completed a year earlier, *i.e.* November 1, 2017. Unfortunately, they were not completed on time.

This prompted a dispute as to whether the deal was still valid. The seller claimed it was defunct once the November 2017 deadline had passed, since the ability to close 12 months later was then precluded. The buyer countered by stating that the closing date was never an essential term; moreover, the deal was still effective since they had agreed it could close on some reasonable future date.

In hearing the dispute, the court agreed that the deal could never have been closed in time for November 1, 2018, once the permit servicing requirements deadline had lapsed exactly one year before.

However, that did not end the matter, since the closing date was never an “essential term” of this Agreement. Indeed, the court found that the parties had mutually agreed in principle to amend the closing date in

the course of their dealings, even though they never signed a written amending agreement or settled on a firm replacement date for closing.

In law, the essential terms of a land sale contract are typically the parties, the price, and the property. The closing date may become an essential term if the parties make it one, but in this case they did not. The evidence here showed that the seller never considered the Agreement to be truly *conditional* on permit servicing requirements being completed by November 1, 2017. This conclusion was bolstered in the correspondence between the parties’ lawyers, where a potential amendment to the Agreement’s closing date was cooperatively discussed.

More to the point, the court noted that the parties had themselves been informally discussing the terms of a written amending agreement, which the seller had drafted and given to the buyer to sign. Their discussions ultimately faltered since the amendments included new terms; in the end, it was never actually executed.

The court noted that at no point did the seller express concern over extending the closing date *per se*. Although he claimed he told the buyer there was a November 1, 2017 deadline to sign an amending agreement, the buyer refuted it and there was nothing in writing. Yet only two days after the deadline, the seller suddenly asserted that the original deal was “frustrated” due to the buyer’s failure to sign the amending agreement. This, in the court’s view, raised questions about the seller’s good faith in the transaction.

The court also pointed out that the seller’s insistence on having a signed amending agreement was reasonable, but the failure to give the buyer *written* notice of any

signing deadline was not.

The court concluded that the seller had no legal right to use the non-delivery of a signed amending agreement as grounds to consider the entire Agreement at an end. The court confirmed the validity of both the original Agreement and the closing date amendments, and declared them binding and enforceable between the parties, in accord with its express written terms. See: *Rolling Meadows v. 2560262 Ontario Inc.*, 2018 ONSC 5063 (CanLII)

Claim to Three Months’ Bonus Interest Found Invalid Post-Maturity

In *Lee v. He*, the court was asked to resolve the straightforward question of whether, in the face of the borrower’s default post-maturity, the lender on a mortgage was entitled to three months’ bonus interest under section 17 of the *Mortgages Act*.

The facts were uncomplicated: The lender advanced \$700,000 to the borrowers, secured by a mortgage on their primary home and on a second rental property. The mortgage had a 12-month term, at which point it was to be paid in full.

The borrowers were unable to pay off the mortgage at the end of the term. After some initial negotiations to renew, the defaulting borrowers went silent, so the lender launched mortgage enforcement proceedings. The lender claimed for \$881,000, representing the total claim for principal, interest, costs, and miscellaneous administrative fees. Included in this amount was approximately \$210,000, part of which reflected the lender’s putative claim for three months’ bonus interest under s. 17 of the *Mortgages Act*. The borrowers

resisted, claiming the fee was illegal given that it was now the post-maturity period.

Before the court, the lender's argument was straightforward: Now that the mortgage was in default, the lender was entitled to either three months' notice of the borrowers' intent to repay it, or else three months' interest by way of bonus under section 17 of the *Mortgages Act*. Since the borrowers were not in a position to pay (having failed to secure alternate financing in the interim), the lender could opt for the bonus interest.

The court disagreed. It observed that mortgages are loan agreements entitling the borrower to use the lender's capital for a stipulated period. In return, the lender is provided with a stream of interest income, together with the ultimate repayment of its capital. When a borrower defaults, the lender is theoretically entitled to not only repayment of its capital, but also the present value of the lost income it would have received by way of interest had the breach not occurred.

That said, the intent of section 17 – which is deemed to be part of every mortgage in Ontario – is to protect the defaulting borrowers by allowing them to pay their arrears without penalty, or else allow them early redemption at a price. It also gives the lender a three-month period during which to arrange for the reinvestment of the principal, or else – *at the borrowers' option* – the payment of money to compensate the lender for not having received proper notice from the borrowers.

The rationale behind section 17 ceases to make sense when a mortgage goes into default after maturity. Then, the lender has already received (or is entitled in law to receive) the whole of the income stream contracted-for. In such circumstances the three months' bonus interest would be nothing more than a penalty, which is something it was never intended to be.

The court conceded that section 17 does not distinguish between defaults occurring *before* maturity, and those occurring *after*. However, every mortgage agreement also entitles the lender to expect repayment on the maturity date; in effect the borrowers are giving notice of an intent to pay on that date. Also, as a practical matter, where mortgages go into default after maturity,

lenders typically institute enforcement proceedings quickly – as was the case here. In doing so, the lender takes the redemption option out of the borrower's hands; the lender cannot then “tack on” an extra three months' bonus interest. In other words, having acted to take enforcement steps, the lender cannot convert the borrowers' option to redeem into an obligation to pay bonus interest.

The court adjusted the amount of the balance outstanding, down from \$210,000 to \$22,000 which still included legal fees and certain modest statement fees. See *Lee v. He*, 2018 ONSC 3656 (CanLII).

Purpose of Condition Not Exercised - Sale Agreement Not Validly Terminated

In *KNRS Acquisitions Inc. v. Fariad*, the court was asked to determine whether a seller had been unreasonable in relying on a “conditional-on-approval” clause to avoid completing a property sale.

The seller had agreed to sell his 12-unit, three-storey apartment building to the buyer. The Agreement contained a clause stating the offer was conditional on its terms being approved by the seller's solicitor, and required the seller to give the buyer written notice in that event. The seller later claimed that this “Solicitor's Approval” clause was added because, although he was the sole registered owner, his mother and brother had a beneficial interest in the property as well, and the brother was refusing to sell. The intent of the clause, according to the seller, was to allow them each a chance to get legal advice on whether a sale could be forced in the face of the brother's opposition.

Tragically, the seller's cousin was murdered in Afghanistan, and the seller's mother immediately flew there to be with family. The seller's brother joined eventually. According to the seller, this made it impossible for him, his mother, and his brother to have the communication with a lawyer as the Solicitor's Approval clause envisioned. He relied on this event to avoid the deal.

The intended buyer sued, and the court was asked to determine whether the Agreement was nonetheless enforceable.

The court found it was. First, it noted that both buyer and seller had a legal duty to act reasonably, honestly, and in good faith, adding that “moral blameworthiness or family dynamics do not factor into the test.”

Next, the court had to evaluate whether the seller had acted in good faith in relying on the Solicitor's Approval clause in view of its particular wording. The only considerations for the court were whether: (1) the termination of the Agreement was achieved in keeping with its provisions, and (2) the seller had acted reasonably overall, in light of the family tragedy.

The evidence showed that soon after the cousin's murder, the seller spoke with the brother, who confirmed his position on not wanting to sell the property was unchanged. It was at this point that the seller advised his real estate agent by text message that he considered the Agreement was at an end. This proved that the trigger for cancelling the deal was the brother's non-consent, nothing more. This flew in the face of the requirement on the seller's part to exercise the clause reasonably, and in good faith.

Indeed, the seller conceded in his evidence that without his brother's consent – which was not forthcoming – he was not prepared to close. This meant that the reason for repudiating the deal had nothing to do with getting the approval of a lawyer, and there was no evidence that either the mother or the brother ever consulted one.

The court added that the wording of the Solicitor's Approval clause was unambiguous on its face, and contained no mention of the mother, the brother, or their consent. The circumstances surrounding the seller's personal family tragedies could not overwhelm its clear wording. Since the seller had not terminated the deal in accordance with the clause (i.e. solicitor approval), the court concluded that the agreement remained valid. See: *KNRS Acquisitions Inc. v. Fariad*, 2018 ONSC 5019 (CanLII).

The statements of law and comments contained in this Newsletter are of a general nature. Prior to applying the law or comments to any specific problem, please obtain appropriate legal advice.