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Mortgage and Real Property Law Report



A Legal Newsletter for the Mortgage and Real Estate Industries

Vol. 25, No. 3 • August 2019

Builder Too Strict in Demanding Evidence of Buyers' Financing

In the Fall of 2016 two buyers, who were spouses, agreed to purchase a yet-to-be-built townhouse condominium from a seller, and tendered an initial deposit. Construction was slated to commence imminently, with occupancy set for Spring of 2019. Due to construction delays, the closing was extended to March of 2020.

The agreement required the buyers to confirm their fiscal wherewithal within 30 days of signing, with evidence that they had the financial ability to complete the transaction on an "all-cash basis" – either wholly from their own savings and investments, or else through third-party mortgage financing. This involved providing the seller with certain evidence, including a copy of their lender's binding, unconditional mortgage or loan commitment, evidence of their annual income, and other personal information.

The buyers duly complied by submitting a letter from their mortgage broker confirming loan pre-approval. At that time, the seller accepted this in satisfaction of the buyers' contractual duty, even though the mortgage was subject to minor conditions.

More than a year later, the seller suddenly introduced new "hoops" for the buyers to jump through, purportedly to satisfy the financing sufficiency clause.

First, the buyers received a letter sent to all 116 purchasers in the townhome project, asking for copies of their binding and unconditional mortgage commitments. Although the buyers complied by tendering theirs, the seller rejected it because the pre-approval came from a broker, not the lender, and was conditional.

The buyers then arranged immediately for a new mortgage commitment, and supplied proof to the seller. That loan also contained a condition respecting the sale of their existing home, so the seller rejected that arrangement as well. The buyers tried again, submitting proof of an unconditional mortgage commitment, but one that listed the wife's parents as co-borrowers. The seller also turned this down since the wife's parents were not parties to the agreement. It refused to let them be added on title.

In April 2018 – which was still a full two years before the scheduled closing – the seller gave the buyers formal notice that it considered them in breach of the agreement. It purported to unilaterally terminate the deal, and keep the deposit.

The buyers sued. The key issue for the court was whether the buyers had adequately demonstrated their financial ability to close the transaction, as the purchase agreement required them to do.

The court noted the buyers had tried to provide the seller with the needed information over the course of many months. This included a pre-approval letter from the mortgage broker and two mortgage commitments from a bank. Despite their increasing frustration at the seller's demands, they also tendered evidence of their savings, RRSPs and TFSAs, investments portfolio, pay stubs, financial statements, and their current property appraisal value. Finally, they also offered a full mortgage commitment with the wife's parents as co-borrowers. The seller was still not satisfied.

Against this background, the court examined the agreement's clause itself. The seller could unilaterally terminate the deal if the buyers failed to provide financial information or procure the needed financing within the stated time-periods. Although the seller had discretion in assessing the sufficiency of the buyers' information, it also had a duty to act honestly and in good faith – which was to be assessed objectively.

The court heard evidence that even at the time of the current hearing, the seller's land was still vacant, which led to the inference that the seller had no true intent to continue building a condominium when it purported to unilaterally terminate the buyers' agreement. As the court put it:

> *[The seller] asked for an unconditional mortgage commitment for the purchase of a unit in a development when ground had not been broken and completion was years away.*

The seller's refusal to accept the two mortgage commitments from the lender bank, and to refuse to allow the wife's parents to be added as co-purchasers, was also unreasonable. Conversely, the buyers' attempts to comply with the agreement, both in providing documentation and providing mortgage commitments were *bona fide* and wholly reasonable. They were entitled to have their deposit returned. See *Ania v. Spice Danforth Inc.*, 2019 ONSC 572.

Buyers Sue Builder Over Builder Invoking Early Termination Clause

Park Avenue Homes Corp. ("Park Ave") was offering pre-construction homes for sale on land owned and developed by 739034 Ontario Inc. ("739"). Park Ave and 739 worked together to develop and build on 739's lands, and entered into a

sub-division agreement with the town to do so.

In 2016, five buyers signed agreements of purchase and sale with Park Ave; they had no contracts with 739. Each agreement was conditional on the timely fulfillment of an Early Termination Clause ("ETC") that required Park Ave to take "all commercially reasonable steps within its power" to obtain various agreements with the relevant Approval Authorities and neighbouring landowners.

Among the required contracts was a Cost Sharing Agreement (CSA) with the unaffiliated owners of the surrounding, still-undeveloped lots that "landlocked" 739's property. The CSA covered the needed infrastructure and road works that would benefit all parties mutually in their various land development plans. Unfortunately these negotiations – for which 739 was solely responsible but which directly impacted Park Ave – took an unexpectedly long time. Ultimately the CSA was only signed in July of 2018.

By early 2017, and with no timeframe for beginning construction, Park Ave realized that 739 would be unable to conclude the CSA within the deadline set in the ETC. Claiming it had met its duty to make reasonable efforts and act in good faith, Park Ave invoked the early-termination portion of the ETC and refunded the five buyers' deposits.

The five buyers sued, and on a motion for summary judgment asked for specific performance and damages. The fundamental issue for the court was whether Park Ave breached its duty of good faith and honest performance in these circumstances. Park Ave argued that it relied on 739 which, as developer, was the only legal entity that could negotiate the CSA and register the subdivision plan that allowed Park Ave's homes to be built. It claimed there was little or nothing it could do to hasten the CSA negotiations along.

The court agreed. In concluding that Park Ave had discharged its good faith obligations, it took into account the reality of the situation. Whether Park Ave's steps were commercially reasonable had to be assessed against the fact that it was reliant on an external event over which it had no real control. By effectively delegating the negotiation and completion of the CSA to 739, Park Ave had acted in a commercially reasonable manner: The two companies were separate, but they communicated regularly and cooperated so that the homes sold by Park Ave could be built.

Turning to the specific efforts by 739 to obtain the CSA, the court found these were significant and *bona fide* as well; they included retaining the assistance of legal counsel and a planner. Although there were some delays in the process, the court noted that perfection is not required to meet the good faith standard or the contractual requirement of commercial reasonableness.

Indeed, it was more honest of Park Ave to notify the five buyers and terminate their agreements in early 2017, rather than hold on to their deposits and continue to wait. The court accordingly dismissed the buyers' claim. See *Li v. Park Avenue Homes Corp.*, 2019 ONSC 1147.

Appeal Court Confirms Buyer's Deposit Forfeited Despite OBCA Protections

A significant ruling we reported on in our December 2018 newsletter (Vol. 24, No. 4) has now been confirmed on appeal.

In *Benedetto v. 2453912 Ontario Inc.* an individual acted as a promoter for a yet-to-be-incorporated company. In that role, he signed a purchase agreement for a $7 million commercial property, stipulating that he was signing as a buyer "in trust for a company to be incorporated without any personal liabilities". He provided a $100,000 deposit to secure the purchase on the pending corporation's behalf.

However, the buyer failed to complete the purchase and the corporation ultimately did not come into existence. Upon the deal being terminated, the promoter asked for the return of the deposit, pointing to the provisions of the *Ontario Business Corporations Act* (OBCA) dealing with pre-incorporation contracts. Those provisions allow individuals acting for a yet-unincorporated company to expressly opt-out of being personally bound by such contracts, and from being found liable for damages.

A lower court had ruled that (absent agreement provisions to the contrary) the promoter's failure to close resulted in the $100,000 deposit being forfeited. The OBCA only protected the promoter from *damages*, or from being bound by the corporation's *contractual obligations*; it did not impact the tendered deposit.

On the buyer's appeal of the trial court ruling, the Court of Appeal affirmed the lower court's interpretation.

The OBCA provisions did contain an "opt-out" provision, allowing the parties to a pre-incorporation contract to expressly circumvent the default rule making promoters liable for contracts they make on behalf of future corporation. But those provisions did not displace the common-law rules governing deposits in real estate transactions. That law states that unless agreed otherwise, any buyer who refuses to close a transaction loses his or her deposit, since it stands not as *damages* for the contractual breach, but rather as *security* and incentive for the buyer's performance. It also compensates the seller for lost opportunity in having taken the property off the market, and for the loss in bargaining power from having revealed the price at which it was willing to sell.

Here, the language of this particular contract – which expressly provided that the promoter was signing the contract "without any personal liabilities" – related to the contract as a whole, but it did not safeguard the deposit in particular. In the context of the entire agreement, it was reasonable for the lower court judge to interpret that phrase as not applying to the deposit at all. It was also noteworthy that the contract had no express provisions to the contrary on how the deposit was to be treated if a breach occurred.

The Appeal Court confirmed that since the promoter had cancelled the deal, the customary law applied so that the $100,000 deposit was forfeited to the seller. See *Benedetto v. 2453912 Ontario Inc.*, 2019 ONCA 149.