

Buyer entitled to repudiate agreement after discovering water damage

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During the period between the time an Agreement of Purchase and Sale (APS) is signed and the completion date, a property being purchased usually remains in the sellers' possession. If damage to the property occurs during that time, a buyer may understandably be concerned about the estimated costs for repairs that cannot be completed before closing. In the event substantial damage has occurred to the property, a buyer has an option to terminate the APS and recover the deposit. However, the conduct of the buyer and seller during this critical period will be closely scrutinized if a dispute winds up in court.

In *Tsui v. Zhuoqi*, 2021 ONSC 5421 (CanLII), the buyers entered into an APS in November 2019 for the purchase of a three-level condominium unit for \$626,800 and paid a deposit of \$31,000. The completion date was scheduled for 10 January 2020.

On 9 January 2020, the buyers attended at the property for a final inspection and discovered that there had been extensive water damage to the floors, subfloor, baseboards, trim, ceiling, and drywall, caused while Kitec plumbing was being replaced.

The next day, the scheduled completion date, the buyers' lawyer wrote to the sellers' lawyer and advised that the buyers required either a holdback of \$100,000 to allow the buyers to repair the damage, or that they be released from the transaction with the sellers paying \$25,000 to cover the cost of temporary rent and buying another property. The buyers were otherwise ready, willing and able to close.

The sellers did not agree to either option. They downplayed the extent of the water damage and proposed that the closing be extended to 13 January 2020, so that the parties could accurately estimate the damage and costs. The buyers were prepared to reduce the holdback to \$80,000 but otherwise maintained their position.

On 13 January 2020, a final effort was made to conclude the sale. The buyers offered to agree to a price abatement of \$75,000 and damages of \$5,000, while the sellers would only agree to a holdback of \$10,000. In support of their position, the sellers relied on an inspection report which estimated the repairs at \$10,000. The buyers requested the opportunity for their engineer to inspect the property, which was rejected by the sellers. The transaction did not close.

In May 2020, the sellers were able to resell the condominium for \$665,000. They claimed that they repaired the water damage before doing so for \$6,893.

The buyers commenced litigation to recover their deposit and for damages. In turn, the sellers alleged that the buyers had breached the APS and forfeited the deposit.

In July 2021, the Ontario Superior Court of Justice heard competing summary judgment motions by the buyers and sellers to determine whose position was correct. The primary issue was whether or not there was "substantial damage" caused to the property allowing the buyers to terminate the APS.

Section 18 of the standard form APS of the Ontario Real Estate Association states (in part) as follows:

18. INSURANCE. The Unit and all other things being purchased shall be and remain at the risk of the Seller until completion. In the event of substantial damage to the Property, Buyer may at Buyer's option either permit the proceeds of insurance to be used for repair of such damage in accordance with the provisions of the Insurance Trust Agreement, or terminate this Agreement and all deposit monies paid by

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Buyer hereunder shall be refunded without interest or deduction.

In a previous case in 2020, the Ontario Court of Appeal determined that a buyer did not have the right to refuse to close a transaction under this section since they had been provided with timely notice of a basement flood that occurred before closing and had the opportunity to inspect the property to determine that the damage was not substantial: *Bilotta v. Booth*, 2020 ONCA 522 (CanLII).

Conversely, the buyers in the case at hand only discovered the water damage 24 hours before closing and there was a real disagreement as to whether or not the damage was substantial. In assessing whether damage is “substantial,” the courts look not only to the estimated cost of repair but to the “quality, character and consequences of the damage”: para 33, citing *Pordell v Crowther Estate*, 2020 ONSC 1635 at para 66.

The court assessed the information that was available to the parties at the time of the aborted closing and determined that it was reasonable for the buyers to have held the view that the repairs could be substantial and well exceed \$10,000. It was not, as the sellers argued, unreasonable for the buyers to seek as much as \$100,000 by way of holdback.

What was unreasonable, in the court's view, was for the sellers to initially refuse to allow the buyers' engineer to assess the scope of the damage, and then to demand that damages be fixed at \$10,000, notwithstanding the limitations of their own inspection report. In doing so, the sellers failed to exercise good faith to take all reasonable steps to complete the sale.

The buyers were therefore legally entitled to terminate the APS and recover their deposit. The court awarded further damages to the buyers for costs associated with the aborted sale of \$33,110, for leasing an apartment while they looked for another property and associated expenses.

The case demonstrates that parties to a real estate transaction must take care to be seen as taking reasonable steps in good faith to ensure that a transaction is completed. While the sellers in the case at hand later allowed an engineer retained by the buyers to inspect the property, their initial refusal to do so was key, as was their refusal to entertain the proposal for a holdback above \$10,000. Had the sellers agreed to a holdback as proposed by the sellers, they may well have received most of the holdback funds once the repairs were completed.

Appeal dismissed: 2022 ONCA 464

In June 2022, the Court of Appeal dismissed an appeal of the decision save for a variation of damages, finding that the motion judge's conclusions on the following facts were entitled to deference:

- The buyers acted in good faith after discovering the damage to the property the day before closing;
- The buyers had good reason to be concerned that the water had caused substantial damage to the property;
- Having regard to the nature, quality, and potential consequences of the damage to the property, that damage was properly characterized as “substantial” within the meaning of s. 18 of the APS; and
- The sellers did not act in good faith in response to the purchasers' discovery of the damage.

Clearly, the buyers had legitimate concerns about the nature and scope of the damage. In that circumstance, the sellers were required to afford the buyers a reasonable opportunity to inspect the property and assess the damage: see also *Bilotta v. Booth*, 2020 ONCA 522, at para. 20. The motion judge properly held that the buyers were not obliged to close the transaction on January 10. Instead, they were entitled to a reasonable opportunity to inspect the property.

The Court of Appeal varied the damages awarded by deducting the costs of the engineering report (\$4,978.89). Otherwise the appeal was dismissed: *Tsui v. Zhuoqi*, 2022 ONCA 464 (CanLII). A PDF version is available to download [here](#).

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