

KEEPING CURRENT

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Relief from forfeiture not granted where buyer claimed lack of capacity to enter into real estate purchase agreement

By James R.G. Cook

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As real estate markets fall, buyers are sometimes left scrambling to find alternate sources of financing when the available mortgage funds turn out to be less than originally anticipated. Without sufficient funding, buyers may be unable to complete the transaction, with sellers having to re-list the property. In such cases, the initial buyer may be liable for damages and will almost certainly lose the deposit even if the seller is able to find another buyer for the property.

Lack of financing is not a valid reason for failing to complete a binding purchase transaction and courts are attuned to the various explanations that a buyer may resort to while attempting to avoid liability to a seller.

The decision of the Ontario Superior Court of Justice in *Mouralian v. Grouleau*, [2022 ONSC 2925 \(CanLII\)](#) illustrates the difficulties that a buyer will encounter when arguing that they should not lose their deposit.

The action arose out of a failed real

estate transaction where the buyer was unable to obtain financing to close the transaction. The seller subsequently resold the property to a third party for more money but nevertheless sought to retain the deposit.

When a buyer fails to close a transaction, the deposit is generally forfeited without requiring proof of any damages suffered by the seller: *Azzarello v. Shawqui*, [2019 ONCA 820](#), at paras. [45-46](#).

In the case at hand, the buyer resisted the seller's claim to retain the deposit on the basis of "relief from forfeiture". Relief from forfeiture is an equitable remedy codified in [section 98](#) of the Ontario *Courts of Justice Act*, which provides that a court may grant relief against penalties and forfeitures, on such terms as to compensation or otherwise as are considered just.

There is a general two-part test to establish relief from forfeiture: (1) whether the forfeited deposit was out of all proportion to the damages suffered;

and (2) whether it would be unconscionable for the seller to retain the deposit.

While the failed transaction caused the seller to incur costs, the property was subsequently sold for more money and the greater sale price more than covered the costs incurred, even if one included the commission on the failed transaction. Since there were no damages, the court therefore assumed that the first branch of the test for relief from forfeiture was made out.

The buyer's difficulty, however, was showing that it would be unconscionable for the seller to retain the deposit. In *Uber v. Heller*, [2020 SCC 16](#), para. [65](#), the Supreme Court of Canada held that unconscionability requires an inequality of bargaining power and a resulting improvident bargain.

In response to a motion for summary judgment brought by the seller, the buyer claimed that her mental state at the time the contract was entered into was affected by the recent death of her close uncle, which triggered memories of the trauma she experienced when her father died in her arms a few years earlier. She was at her uncle's funeral when her real estate agent allegedly pressured her into signing the offer to purchase the property.

While the seller did not sign back the offer until the next day, the buyer claimed that as a result of the combination of the pressure her real estate agent placed on her, and her severe emotional distress, she lacked the capacity to agree to the terms of the agreement of purchase and sale ("APS").

The motion judge noted that a party seeking to escape the terms of a contract on the basis of mental incapacity must generally show not only that they were mentally incompetent, but also that the other party knew or at least was aware

of facts that should have put them on notice that the person's state of mind was in question: *e.g.* *Lougheed v. Ponomareva*, [2013 ONSC 4347](#), at paras. [43-45](#).

The buyer did not have any persuasive, contemporaneous medical reports to support her position. Further, it was also clear that the seller had no knowledge of any alleged incapacity of the plaintiff at the time the APS was signed. The parties had no prior relationship. Each side had an independent real estate agent advising and negotiating the APS for them. There was no evidence that the buyer had taken any steps to repudiate the transaction after signing the APS. Indeed, she had taken active steps towards the closing until her means of financing fell through.

Accordingly, the motion judge found that there was no inequality of bargaining power.

The buyer was also unable to show that the transaction was improvident. The fact that the property re-sold for an even higher amount suggested that the sale price the parties agreed to was at least fair. The deposit in question—typical for a residential property transaction—was in the amount of \$70,000, representing about 5% of the agreed-upon sale price of \$1,499,000.00.

As a result, the seller's motion was granted and the buyer was liable for breach of the APS. The deposit and accrued interest was forfeited to the seller.

As noted in the decision, the reality was that litigation arose because the buyer encountered some unfortunate circumstances which, despite her best intentions, impacted her ability to obtain the financing she needed to close the purchase. However unfortunate, a buyer's personal



circumstances do not lead to the conclusion that it would be unconscionable for a seller to retain a deposit. A deposit is not a windfall for a seller because it is not meant to be damages for the failed transaction, but rather it is security to “incentivize” buyers to close a transaction.

Contact us

If you have a litigation matter and are in need of legal advice, please do not hesitate to contact James Cook, at 416.865.6628 or jcook@grllp.com.

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