DE FRANCESCA LAW

REAL ESTATE AND MORTGAGE REPORT

BI-MONTHLY NEWSLETTER

EDITORIAL BOARD: PAUL DE FRANCESCA, AMANDA CARPENTER, ZEESHAN BAIG

Volume XV Number 1 February 2020

DEPOSITS:

Forfeiting Deposits: Signing APS "in Trust" for a Company to be Incorporated Doesn't Help

In *Benedetto v. 2453912 Ontario Inc*. [2019] argued before the Ontario Superior Court of Justice and later the Court of Appeal, the case dealt with an agreement of purchase and sale ("APS") for three adjacent Toronto properties at a purchase price of $7.0 million. The APS in question was signed by the purchaser personally "in trust" for a company to be incorporated without any personal liabilities. The APS was firm with the purchaser paying a deposit of $100,000. Two weeks prior to closing, however, the purchaser elected not to proceed with the transaction and requested the return of his deposit.

The motion judge provided an analysis of deposits, concluding:

(i) Where a payer (usually the purchaser) provides a vendor with a deposit to secure the performance of a contract for purchase and sale of real estate, the deposit is forfeit in the event the purchaser refuses to close the transaction, unless the parties bargained to the contrary, and

(ii) The deposit stands as security for the purchaser's performance of the contract. The prospect of its forfeiture offers an incentive for the purchaser to complete the purchase. Should the purchaser not complete the transaction, the forfeiture of the deposit compensates the vendor for lost opportunity in having taken the property off the market in the interim, as well as in the loss in bargaining power due to the vendor having revealed to the market the price at which the vendor had been willing to sell.

The motion judge further stated that a deposit is not part of the contract of purchase and sale, but rather "stands on its own as an ancient invention of the law designed to motivate contracting parties to carry through with their bargains."

While the vendor relied on settled precedent that failure to close a real estate transaction results in the forfeiture of a deposit, the purchaser chose to take a more novel approach to the matter. Namely, they attempted to rely on section 21(4) of the *Ontario Business Corporations Act*, R.S.O. 1990, c. B.16. Section 21(4) of the Act provides that "[if] expressly so provided in the oral or written contract…a person who purported to act in the name of or

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on behalf of the corporation before it came into existence is not in any event bound by the contract or entitled to the benefits thereof."

Therefore, in the event of a breach of a pre-incorporation contract where s. 21(4) applies, where the purchaser advised the vendor that he would not be completing the purchase, the vendor has no remedy for the breach. In other words, the vendor cannot claim damages against the intended corporation as the intended corporation – even if it ever came into existence - did not adopt the contract.

On appeal, the Court of Appeal held that it was reasonable for the motion judge to interpret the phrase "without any personal liabilities" in the context of the contract as a whole, as not applying to the deposit specifically. In essence, a forfeited deposit stands as security for the performance of the contract. An implied term of a deposit is that on breach of the contract by the purchaser – or, in the case of a pre-incorporation contract, by the promoter on behalf of the intended purchaser – the deposit is forfeited to the vendor.

For real estate investors, this decision is helpful as it is commonplace to see in an APS for the buyer named in the APS in trust for a company yet to be incorporated without any personal liability. Although a buyer may be able to avoid a claim for damages by a seller if and when the purchaser defaults, the buyer will clearly still forfeit the deposit.

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