

Legal

Backing Out of Construction Contracts



With the current economic downturn and with a number of large condominium projects nearing completion in the City of Calgary and elsewhere in the province, frequent questions have recently been raised by both industry members and purchasers concerning the consequences of not completing a new condominium purchase.

A number of different remedies including specific performance, forfeiture of deposits and damages may be available to the developer. Industry members are strongly urged to always refer these types of questions to a solicitor. For the purposes of dispelling some common misconceptions only, this article addresses some of the consequences of a buyer reneging on a binding contract.

First of all, it should be noted that condominium construction/purchase agreements are typically tailor-made by the developer's solicitors to represent the best interests of the developer and as such, they rarely afford an opportunity for the buyer to not complete the purchase, even if excessive delays in the construction of the project or some other breaches of the developer's obligations are perceived by the buyer to have occurred. If the buyer unilaterally elects not to complete the transaction, then some of the agreements will allow the developer to "accelerate" the payment of the balance of the purchase price and/or keep any and all funds paid by the buyer to the date of default. Rarely, however, do the agreements limit the developer to the forfeited deposits as a genuine pre-estimate of the damages and usually a cause of action for any additional losses (damages) is available against the buyer. These losses can be quite substantial in the current buyer's market, where prices are declining and where it may take the developer some time to resell the property to another buyer for a reasonable price.

The recoverable damages could include any and all of the following:

- ❖ loss of resale value (provided that the builder acts reasonably to "mitigate" the loss)
- ❖ extra advertising expenses
- ❖ legal costs incurred by the developer arising from the default
- ❖ extra real estate commissions paid
- ❖ all carrying costs for the time period from the original closing date to the ultimate re-sale date including financing interest, condominium fees, property taxes and utilities.

In conclusion, a buyer should never be advised that they can walk away from a construction agreement and simply lose the deposits paid on the transaction to date. In most instances, it will be better for the buyer to complete the purchase and either rent or re-sell the property themselves in order to minimize the financial losses suffered.

Cash Back Deals

A new development in the market has come to my attention recently. Twice in the past couple of weeks, I have been approached by buyers with purchase contracts (with different developers) where the price was inflated by \$40,000 to \$50,000 to show a higher price on the face of the agreement. In the portion of the contract showing how the price is paid, there is a corresponding "cash back" on closing provision.

Why is this happening? Developers may want to create the illusion that the new home market is not in distress or they may want to give the impression that they are not undercutting their competitors.

While this is not mortgage fraud because it is transparent on the face of the agreement (i.e. it's not a side deal), it nevertheless creates several significant problems that made me advise the buyers not to execute the agreements. I certainly would not be prepared to act on the transaction.

Here are the problems from the buyer's perspective:

- ❖ The property taxes will be inflated for years and the buyer will not be able to appeal the tax assessment
- ❖ On the GST rebate application (if applicable), there are declarations that the application reflects the true purchase price paid. To complete the application in these circumstances would likely constitute fraud
- ❖ In recognition of the GST rebate problem, the developers in these circumstances are not giving the buyer a "net of GST rebate" price but instead requiring the buyer to apply for the GST rebate refund to the government
- ❖ On submitting the transfer of land to Land Titles, the buyer is required to execute an affidavit of value, based on what the buyer believes the property would be likely to sell for on the open market. Land Titles will not accept a valuation of less than the purchase price reflected on the face of the transfer of land. If the buyer swears that the purchase price reflects true value, then once again, the buyer is likely committing perjury.

A REALTOR®, whether acting for the developer or for the buyer, would not be doing anything illegal by participating in such a scheme, but the buyer's agent might face liability risks if the consequences of this type of transaction are not fully explained to the buyer.

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