

When the Deal Goes South: Deposits, Unconscionability, and Relief from Forfeiture

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Recent cases from the Ontario Court of Appeal address issues regarding deposits in failed purchase and sale transactions. An examination of these cases provides guidance regarding the circumstances in which the forfeiture of a deposit may be deemed to be unconscionable, and the circumstances in which a court may be moved to grant relief from forfeiture.

Deposits and Relief from Forfeiture

In a purchase and sale transaction, the purchaser often pays an amount of money in advance as a deposit. The theory is that a deposit will motivate the contracting parties to complete the transaction. If the contract is performed, the deposit is applied to the purchase price. Conversely, a deposit is generally forfeited by a buyer who repudiates the contract. However, the court has the discretion to grant relief from forfeiture in circumstances that it considers appropriate.

The jurisdiction to grant relief from forfeiture is succinctly stated in s. 98 of the *Courts of Justice Act*. It provides: “A court may grant relief against penalties and forfeitures, on such terms as to compensation or otherwise as are considered just.”

To assess whether relief from forfeiture is appropriate, the Court of Appeal has adopted a two-step test: (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: *Varajao v. Azish*, [2015 ONCA 218](#) (para. 11).

Jensen v. Chicoin

In *Jensen v. Chicoin*, [2018 ONCA 793](#), the Court of Appeal upheld the trial judge’s finding that the \$100,000 paid toward the agreed-upon purchase price of \$500,000 was a deposit that could be retained by the seller when the transaction for the sale of a small business that supplied and installed granite countertops broke down without legal fault on either side. The parties had entered into a one-page termination agreement that, although it did not specifically refer to the \$100,000, reflected an intention that the funds would stay with the seller.

The trial judge in *Jensen* ([2018 ONSC 95](#), paras. 42-50) declined to grant relief from forfeiture. In finding that it would not be unconscionable for the seller to retain the deposit, the trial judge made various findings that included the following: (1) both individual parties previously ran their own businesses and the evidence did not show an inequality of bargaining power; (2) the acquisition arrangements were negotiated over an extended period of time; (3) the parties chose not to involve legal professionals in drafting the transaction documents to their apparent mutual disadvantage; (4) the termination of their relationship involved trade-offs by both parties; and (5) the consequences were not substantially unfair to one party over the other.

Redstone Enterprises Ltd. v. Simple Technology Inc.

In conducting his analysis, the trial judge in *Jensen* had regard to the Court of Appeal's decision in *Redstone Enterprises Ltd. v. Simple Technology Inc.*, [2017 ONCA 282](#). In *Redstone*, the Court of Appeal overturned the application judge's decision to grant partial relief from forfeiture where an initial deposit of \$100,000 grew to \$750,000 on a purchase price of \$10,225,000 in a real estate deal for the purchase of a warehouse that was to be used for a licensed marijuana grow-op business. The deposit increases were occasioned by the purchaser waiving conditions and requesting an extension of the closing date. Ultimately, the purchaser was unable to obtain the licence and financing it needed to proceed. The application judge found that complete forfeiture of the \$750,000 would be unconscionable in the absence of any evidence concerning damages suffered by the vendor.

For its part, the Court of Appeal in *Redstone* found no unconscionability in the vendor retaining the full \$750,000 deposit. Among other factors, the Court of Appeal noted that: (1) the full deposit was just slightly more than 7% of the purchase price; (2) the deal was a commercial real estate transaction between strangers; (3) both parties were sophisticated; (4) there was no inequality of bargaining power; and, (5) the increase was negotiated.

In *Redstone*, the Court of Appeal noted that the analysis of unconscionability requires the court to step back and consider "the full commercial context" (para. 18). The Court opined that "the finding of unconscionability must be an exceptional one, strongly compelled on the facts of the case" (para. 25). Nevertheless, the Court conceded that "in some circumstances a disproportionately large deposit, without more, could be found to be unconscionable", although the dispute before it was not such a case (para. 26).

Scicluna v. Solstice Two Limited

The Court of Appeal did encounter what it found to be an unconscionably large deposit in *Scicluna v. Solstice Two Limited*, [2018 ONCA 176](#). There the Court dismissed an appeal from the application judge's decision to grant relief from forfeiture. Ms. Scicluna had paid close to 80% of the total purchase price for a condominium unit: \$293,685 on a total purchase price of \$372,000. After losing her job, she was unable to pay the remaining balance. Solstice then found itself able to sell the same condominium unit to another purchaser for a higher price, \$435,000. Solstice sought to retain both Ms. Scicluna's \$293,685 deposit and the additional profit that it made on the resale.

The application judge found Ms. Scicluna's \$293,685 deposit to be "out of all proportion to the losses suffered" by the vendor such that it would be "unconscionable" for Solstice to retain the full amount of the money. The Court of Appeal similarly found the "substantial disparity" between the value of the property forfeited and the damage caused to Solstice by the breach to be "so manifest and so grossly disproportionate" that relief from forfeiture was "patently a correct result". Accordingly, it dismissed the appeal and relief from forfeiture was granted.

Unconscionability: Relevant Factors

The *Scicluna* decision demonstrates that cases do exist in which the gross disproportionality in the size of a deposit will be enough to establish unconscionability. However, such cases will be rare. *Jensen* and *Redstone* reflect the more typical situation in which a court must engage in a contextual analysis to determine whether it would be unconscionable for a vendor to retain the deposit such that relief from forfeiture is appropriate.

The Court of Appeal in *Redstone* stated that "[t]he list of the indicia of unconscionability is never closed, especially since they are context-specific" (para. 30). But the decisions in *Jensen* and *Redstone* provide helpful examples of what is involved in a contextual analysis to determine unconscionability. Such an analysis will have regard to many factors, including: (1) the relative bargaining power of the parties; (2) the parties' relationship; (3) the parties' comparative sophistication; (4) whether *bona fide* negotiations took place; (5) the nature of the transaction; (6) the overall fairness of the bargain; (6) the gravity of the breach; and, (7) the conduct of the parties.

Conclusion

Issues concerning deposits, unconscionability, and relief from forfeiture inevitably turn on the context and specific facts of a particular dispute. The decisions in *Jensen*, *Redstone*, and *Scicluna* provide helpful guidance in identifying the relevant factors and the evidence that must be marshalled to conduct the necessary analysis to determine the outcome in a given case. Although freedom of contract and certainty in the marketplace dictate that findings of unconscionability must be the exception, strongly compelling facts will persuade a court to grant relief from forfeiture.

The information and comments herein are for the general information of the reader and are not intended as advice or opinion to be relied upon in relation to any particular circumstances. For particular application of the law to specific situations, the reader should seek professional advice.

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