

## on account of damages: doesn't always mean that damages must first be proven

A recent decision of the British Columbia Court of Appeal, released February 5, 2013, has held that where a buyer has paid a deposit with respect to the purchase of real property and then subsequently fails to complete the transaction, the deposit will be forfeited by the buyer without the seller needing to prove damages provided the contract states that the deposit will be forfeited "on account of damages."

In *Tang v Zhang*,<sup>1</sup> the sellers entered into a standard form contract used by the Greater Vancouver Real Estate Board to sell a residential property for \$2,030,000. The contract contained the following provision:

"TIME: Time will be of the essence hereof, and unless the balance of the cash payment is paid and such formal agreement to pay the balance as may be necessary is entered into on or before the Completion Date, the Seller may, at the Seller's option, terminate this Contract, and, in such event, the amount paid by the Buyer will be absolutely forfeited to the Seller in accordance with the Real Estate Services Act, on account of damages, without prejudice to the Seller's other remedies." [Emphasis added.]

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<sup>1</sup> *Tang v Zhang*, 2013 BCCA 52.

The buyer paid a deposit of \$100,000 to the real estate agent but then failed to complete when required. The sellers took the position that the \$100,000 deposit became absolutely forfeited to them on account of damages, without prejudice to their other remedies and demanded that the buyer consent to the real estate agent's release of the deposit to them. The seller was subsequently able to sell the property to a third party at a higher price, with the result that they did not suffer any (pecuniary) damages.

In deciding whether the deposit was "non-refundable and forfeited without proof of damages," the court followed previous authority supporting the proposition that "the interpretation of whether a deposit clause is refundable or non-refundable depends on the specific wording of the contract of purchase and sale." However, when interpreting a clause in an agreement, it is not sufficient to look only at the wording of the clause in order to decide on its meaning and application; instead the clause must be examined in its place in the agreement as a whole. Further, the agreement as a whole, and the clause in particular, must be examined in the context of the factual matrix which gave rise to the agreement and against which the agreement and the clause was intended to operate. With respect to the case at hand, the court found that in the absence of a manifest contrary intention, the words used in the document must be construed in light of their meaning at common law.

In *Howe v Smith*<sup>2</sup>, the English Court of Appeal found that a deposit is a guarantee that the contract should be performed. This was based on the fact that if the sale proceeds, the deposit would be applied towards the purchase price, however, in the event the purchasers default on their obligation to complete, the deposit is forfeited. In this way, a deposit is not merely a part payment of the purchase price, but is also an intention to bind the parties; by creating a fear of its forfeiture, the deposit instills

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<sup>2</sup> *Howe v Smith*, (1884) 27 Ch. D. 89.

a motive in the buyer to perform the rest of the contract. This line of reasoning has been adopted by the Supreme Court of Canada and remains the seminal authority on deposits in the context of real estate transactions.

Based on the foregoing, the court found that although the phrase "on account of" is sometimes used in place of "because of" and can be limiting in nature, in the context of a standard form legal document, the phrase is intended to mean that in any action by a vendor to recover damages against a defaulting purchaser for breach of a contract, the amount of the deposit would be counted towards such damages. Essentially, the court found that the purpose of the phrase is to prevent double recovery if damages are proven, not to require proof of damages before recovery. This is consistent with the principle that the nature of the deposit is a guarantee of performance in place to encourage contracting parties to complete their contracts in accordance with their terms. As such, purchaser's counsel and real estate agents should ensure their clients are aware of the risks in losing their deposit should they fail to complete the purchase of a residential property, and ensure that the conditions precedents contained in the contract adequately protect the purchaser so that they are able to walk away from a deal should the need arise.

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the contract, which the court concluded would have been the only possible remedy.

As these provisions demonstrate, lenders and borrowers should remain alert to the range of rules contained in Canadian legislation and case law that govern the rate of interest payable. We would be pleased to assist lenders and borrowers with these matters.

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