Property Newsletter

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Introduction

This edition of the CBP Property Newsletter is larger than normal as we have tried to highlight the variety of ways purchasers are now trying to withdraw from contracts in these difficult economic times where they have purchased off the plan and the market has significantly changed since contracts were entered into.

We trust you find these case studies interesting. A major lesson to take on board is ensuring attention to detail. When times are tough financially and purchasers are looking for ways to withdraw from contracts, it is a lack of attention to detail that often affords them the opportunity to do this. This has disastrous consequences for the developer who is relying on committed pre-sales to make the project viable and to secure funding.

Deposits less than 10%

Most of you will recall our previous articles on the decisions in 2006 and 2007 respectively in *Luu v Sovereign Developments Pty Limited* and *Iannello v Sharpe* which dealt with payments of deposits of less than 10% and where, calling for a later payment of part of the deposit to bring it up to 10% when the purchaser defaulted amounted to a non-enforceable penalty.

To try and overcome the effect of the decisions, many contracts have been drafted on the basis that the deposit is payable by two instalments, with the first instalment being the amount that is handed over on exchange and the second instalment being the balance of 10% which is payable at the time completion is due.

It has been our belief (and our advice to our clients) that this is not a genuine instalment arrangement with respect to the deposit and would be struck down by the Courts on the basis that the second payment amounts to a penalty.

This view of our firm has been supported by the recent decision of *Boyarsky v Taylor* where the Court held that a clause which stated that the deposit was 10% but payable by two instalments, with half being payable at the date of exchange and half on the completion date as defined in the contract was not enforceable. This attempt by the vendor to secure payment of the balance of the 10% deposit when the purchaser defaulted amounted to a penalty and would not be allowed.

Effectively, notwithstanding the special condition in the contract, the Court held that the second payment could only in reality come in effect when the purchaser defaulted and did not settle on the due date.

The vendor tried to argue that the second payment was not necessarily tied into a breach of the contract by the purchaser and payable on that breach occurring, as the vendor could agree to extend the time for settlement but the second instalment of the deposit would be payable at the time settlement should have occurred.

This argument was given short shrift by the Court. Any such arrangement would involve a variation of the contract, would need to be documented and, if the arrangement was that the balance of the 10% deposit had to be paid as consideration for the variation, then this could be documented at that time.

On a strict interpretation of the contract, the only circumstances where the second half of the deposit would be due would be where the purchaser did not settle by the completion date set out in the contract and was in breach of the contract.

Therefore, the second instalment of 5% of the deposit was not a genuine pre-estimate of damage, was a penalty and not recoverable by the vendor.

As previously advised, vendors have to very carefully consider whether to accept an exchange with a deposit of less than 10%. If the vendor does so, unless there is a genuine instalment arrangement for the deposit (ie where the deposit is 10% payable in tranches on given dates and before the completion date), then all the vendor is likely to be able to recover if the purchaser defaults is the deposit paid on exchange.

The decision of *Luu, Iannello* and *Boyarsky* show that the Courts consider that, in circumstances where vendors accept less than 10% as a deposit, the vendor has made a conscious, commercial decision to accept a lesser deposit as an earnest for the purchaser's commitment to buy the property.

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Extensions of time for registration of plans

When buying off the plan, contracts will often stipulate a sunset date. If the plan is not registered by the sunset date, the parties may terminate. Often the contract gives the vendor the right to extend the sunset date for matters beyond his or her control.

The decision in *Cockburn & Ors v Key Urban Pty Limited* looks at extensions sought by a vendor and whether the notice of extension was valid.

This case involved a group of purchasers who bought units at Campbelltown off the plan.

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The sunset date for registration of the plan was 1 October 2007. Prior to this date the vendor sought to obtain extensions of time by giving notice under a special condition in the contract. This special condition allowed for extensions of time where the vendor or builder were delayed in completing the construction due to various nominated matters (eg inclement weather, industrial disputes, etc) and "any matter beyond the control of the vendor".

On 30 March 2007, the vendor informed the conveyancers acting for the purchasers that it had to refinance as its first financier had been placed in administration. This meant that the project had stopped and the vendor claimed an extension of time.

In claiming extensions of time, the vendor was required by the new lender to seek an extension not just for the number of days lost due to this unforeseen circumstance (314 days), but for a significantly longer period of time required by the mortgagee as a "safety buffer". The vendor therefore claimed a total extension of 548 days.

The purchasers rejected the validity of the notice and sought to rescind their contracts and have their deposits repaid. The vendor rejected the validity of the rescission notices and maintained that the purchasers were bound to complete.

The Court held that special conditions relating to extension of time have to be construed strictly. It followed that the vendor was only entitled to claim an extension for the actual period by which the project had been delayed, not some greater period.

The Court held that the vendor's notices were ineffective to extend the date for completion. It declined to read the notices liberally to grant the vendor the period of 314 days which was acknowledged as the period by which the project had been delayed.

The purchasers were held to have been correct in rescinding the contracts and we are entitled to have their deposits returned.

The vendor's next contention was that, as each of the purchasers had engaged an agent to resell the units, they had effectively elected to treat the contracts as still being on foot or had affirmed the contracts.

The Courts did not accept this, saying that all the purchasers were doing was effectively "covering their bases". The mere engaging of agents and advertising of units for sale was consistent with the purchasers' claim that they had validly rescinded the contracts.

The decision in this case, like the decision in *Chin v Frances Park (Darwin) Pty Limited* (referred to elsewhere in this bulletin), suggests that the Courts tend to construe strictly the contractual

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provisions drafted by the vendor for the vendor's benefit. It is important for vendors to pay close attention to the exact wording of special conditions when seeking to give notices under a contract.

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Clause 7 claims

Clause 7 of the standard contract for sale of land used in New South Wales sets out a regime where, if a claim is made for an amount greater than 10% of the purchase price, the purchaser can make a claim prior to settlement and the vendor can elect to either rescind the contract or set aside the amount of the claim (up to 10% of the purchase price) which is then arbitrated on after the matter settles.

The recent Court of Appeal of the Supreme Court of New South Wales decision in *Nassif v Caminer* considered this clause and how it applies to various purchaser claims that arise between exchange and settlement.

This matter involved the sale of a property which was subject to a substantial lease. The property was advertised as being subject to a secure lease with three years left to run and a gross income of $384,000 per annum.

Prior to exchange, the purchaser asked the vendor's agent whether the tenant was a good tenant and the agent replied that the tenant was a secure tenant and it was only in arrears for the last month's rent.

It became apparent between exchange and settlement that this representation was false. The tenant in fact had gone into liquidation soon after exchange and appears to have been several months in default at the time the property was put up for sale by way of auction.

One clause in the contract (clause 49) stated that the purchaser had satisfied itself in respect of all matters relating to the terms, nature, status and enforceability of the lease and that the purchaser was not entitled to delay completion, object nor make requisitions or claims in relation to the lease.

When, just prior to completion, the purchaser discovered the real situation with respect to the tenant, the purchaser's solicitor made a claim under clause 7. The vendor rejected the claim and relied on special condition 49 of the contract. The purchaser then refused to settle and sought to rescind the contract. The vendor accepted the purchaser's rescission as a repudiation of the contract and itself terminated the contract and sought to forfeit the deposit.

The Court of Appeal overturned the decision at first instance and held that the purchaser's claim based on the alleged misrepresentation

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prior to the contract did not fall within clause 7 of the contract and therefore the purchaser had purported to terminate the contract without any just cause.

The Court held that the ordinary meaning of "claim" in clause 7 was extremely wide. This word did not, on its proper construction, extended to the purchaser's claim in this matter because of the terms of special condition 49 which precluded the purchaser from making any claim in relation to the lease.

The Court held that there must be a logical connection with the contract to any claim made and there is no logical basis for excluding from the ambit of "claims" one based on false and misleading representations.

The broad words in clause 49 "in relation to" included any pre-contractual representations or misrepresentations. Clause 7 does not itself specify any particular form for a claim to be made. The only requirement is that it must contain a statement of the amount claimed. The purchaser's solicitor's letter satisfied this requirement and was a claim for the purposes of clause 7, which the purchaser was not entitled to make and therefore the purchaser had repudiated the contract. Therefore the vendor was entitled to terminate the contract and forfeit the deposit.

The Court noted that any claim under clause 7 of the standard contract terms must have a reasonably arguable basis and not be made in bad faith. However the Court acknowledged that the procedure under clause 7 can only be initiated by the purchaser.

In this case, the purchaser was precluded from making a claim by virtue of the provisions of clause 49 and therefore could not make a valid claim under clause 7.

The Court held that the issues of the tenant's capacity to pay and the extent of the rental arrears were matters which "related to" the lease and therefore were covered by special condition 49.

The Court seemed to acknowledge that the purchaser may have had (and may still after the proceedings have had) an entitlement to bring separate proceedings under the *Fair Trading Act, the Trade Practices Act* or at common law for the alleged misrepresentation but this did not assist the purchaser in these proceedings as the purchaser had elected to rely upon clause 7 (which it was not entitled to do).

By a majority of two to one, the Court elected not to exercise its discretion to return the deposit to the purchaser under section 55(2A) of the *Conveyancing Act,* acknowledging that a Court will not likely order the return of a deposit where a purchaser has defaulted.

The purchaser tried to argue that the fact that the property had been resold at a higher price was a material matter which should have led to an order for return of the

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deposit. The Courts acknowledged that this one factor to be taken into account but was not the sole factor.

The fact the purchaser had only paid a 5% deposit rather than the normal 10% deposit also militated against a return of the deposit.

Parties must therefore be very careful when making claims for misrepresentation under the contract and must appreciate the difference between making a claim under clause 7 and making a statutory claim or a claim at common law for misrepresentation (which may give rise to an entitlement to damages but not termination of the contract).

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Sales subject to reports

The Northern Territory decision of *Chin v Frances Park (Darwin) Pty Limited* highlights the care required when making contracts subject to various reports.

In this matter, the purchaser was to acquire three lots on which there was previously an oil storage facility operated by BP Australia.

A special condition in the contract stated the contract was conditional upon the vendor providing the purchaser with written confirmation from an accredited environmental auditor that the properties were suitable for residential use. The same special condition required the implementation of a groundwater monitoring and management plan.

The purchaser wanted to rescind the contract on the basis that the condition requiring confirmation the properties were suitable for residential use had not been met. A report prepared for the vendor by a consultant stated that certain things had to be done before the land would be suitable for residential use.

The purchaser argued it was entitled to rescind on the further ground it was not provided with the report, as required by the special condition. The report was merely given to the vendor by the consultant.

The Court found in favour of the purchaser on both issues and ordered a refund of deposits.

Eventhough the special condition, when read literally, did not require the written confirmation to be addressed to the purchaser, the Court held that the intention was that the statement should have been addressed to the purchaser to reassure the purchaser it could proceed with settlement.

It was also held that the groundwater condition was not an extension of the condition requiring confirmation the properties were suitable for residential use but was a further condition in its own right.

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Care must be taken when drafting conditions to provide purchasers with reports or evidence. You should consider exactly who is to receive the reports or evidence and what the reports or evidence are to state. Also, the groundwater monitoring programme should have been covered by an "ancillary matter" extension to the special condition. Because it was not specifically referred to, the purchaser was able to validly rescind the contracts.

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Requisitions in sale matters

The question of what is a valid requisition is a vexed one.

They are often called "requisitions on title", but the Courts have held a purchaser can make valid requisitions on matters other than title.

In the matter of *Wood v Lyons*, the vendors were selling a property at Killarney Heights for $1,130,000. The purchaser failed to settle on time and a notice to complete was issued.

Extensions of time to settle were given as the purchaser's funds from England were delayed.

After a number of extensions, the vendors terminated the contract and sought damages.

Prior to entering into the contract, the vendors had applied for a building certificate from Warringah Council. After exchange, the Council issued a letter which detailed works that needed to be done or information that needed to be provided.

The purchaser made requisitions which were only responded to a few days prior to the completion date.

The purchaser pointed to the fact of the issue of Council's letter and the replies to requisitions as not entitling the vendor to issue a Notice to Complete. He contended that the vendor, in purporting to terminate relying on the purchaser's failure to settle under that Notice, had repudiated the contract.

The purchaser claimed that because of the Vendor's repudiation, the purchaser was entitled to terminate the contract and had a right to claim back the deposit.

The requisitions relied upon by the purchaser were to the following effect:

- Whether the provisions of the *Local Government Act* and the ordinances under it with regards to subdivision and buildings have been complied with (answered

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by the vendor "yes as far as the vendor is aware").

- Whether all the requirements of the *Local Government Act* and the ordinances under it relating to alterations or additions to any structure on the property have been complied with (answered by the vendor that the purchaser had to rely on his own enquiries).
- Does the vendor hold, or is the vendor aware of, a certificate of compliance under the *Local Government Act* (responded to "no")?

The Court held that the answers to the first and third requisitions were acceptable whereas the answer to the second question was too broad and was not permissible.

It was held that, generally, the response "purchaser must rely on its own enquiries" is an insufficient response, whereas a response "not so far as the vendor is aware but purchaser should make his own enquiries" is permissible.

Fortunately for the vendor, the second requisition referred to above was held to be too broad. The requisition referred to all of the requirements of the *Local Government Act* and the ordinances under it. It was unreasonable to expect the vendor to go through all of this legislation to see what applied to his property and then work out how he should deal with each and every issue as it applied to his property.

The Court held that all of the requisitions had either been adequately answered or were not permissible.

The purchaser's next contention was that the notice to complete should have set out all of the vendor's rights on termination whereas it merely indicated that the vendor would be entitled to terminate the contract. The purchaser maintained that the notice should have said that the vendor would resell the property, that the deposit would be forfeited and the vendor would seek damages (and the type of damages that the vendor would seek).

The Court held that this was nonsense because standard clause 9 clearly sets out the consequences of the purchaser's default. The vendor did not have to repeat what was in this clause in the notice to complete.

The purchaser then claimed the vendor had an obligation to disclose that he had made an application for, but had not yet received the building certificate as at the date of the contract. The Court held there was no such obligation on the vendor.

Therefore, the vendor had validly terminated the contract and was entitled to damages.

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This matter represents a clarification as to the type of requisitions that can be raised, what constitutes proper requisitions and the proper answers to requisitions.

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Conditions precedent to settlement

The recent Supreme Court of New South Wales decision of *Kaljo v Coady* is a reminder of the care required when negotiating and documenting conditions in contracts, particularly where they are a condition precedent to settlement.

The vendor was selling a property at Warwick Farm which was subject to a charge in favour of Liverpool Council.

The contract contained a special condition which disclosed the existence of the charge and stated that completion was conditional on the purchaser entering into a deed of release and indemnity with the Council.

The charge had been entered into to address the Council's concern there might be liability issues with flooding of the land. The deed of release and indemnity provided the Council could not be held liable for damage or loss arising from flooding.

Council would only agree to enter into a deed with the purchaser if the purchaser's mortgagee was a party to the deed and gave a similar indemnity to Council.

The purchaser, through her finance broker, spoke to a mortgagee which indicated it would not enter into such a deed. The broker, rather than seeking finance from other lenders to see if they were prepared to meet the requirements of the Council, tried to negotiate the matter with the Council and its solicitors, without success.

The time for settlement had expired and under the standard clause 29 of the contract, if an event set out in a contract has not happened by the relevant date in the contract, then either party can rescind within seven days.

The purchaser did not seek to rescind within that seven day period and eventually the vendor issued a notice to complete which the purchaser disputed.

The purchaser then purported to rely on clause 29 of the standard contract to rescind the contract on the basis that the precondition for settlement (finalising the arrangement with Council) had not been met. She sought a refund of her deposit.

The Court held that the special condition was not for the benefit of one party to the exclusion of the other. The clause gave a benefit to both parties to rescind if the arrangement with Council could not be finalised.

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The vendor alleged that the purchaser could not rescind as the purchaser was in breach of clause 29.4 — she had not done everything reasonably necessary to have the condition satisfied. She should have approached a number of mortgagees to find a mortgagee that would accept Council's conditions in relation to entering into the deed and giving the discharge of the existing charge over the property. The Court did not accept this as the special condition only contemplated a deed being entered into between two parties — the purchaser and Council — not any mortgagee.

As the Council indicated it was not willing to enter into a deed between just itself and the purchaser, the Court was satisfied the purchaser had done all she had to do to satisfy this condition.

The vendor argued that the purchaser had lost her right to rescind as she had not done so within seven days of the expiry of the six week period.

The Court held that the parties had both, after the expiry of this period, treated the contract as if it were still on foot. This meant the purchaser's right to rescind was not lost. It followed that the vendor was not entitled to issue a notice to complete and, because the provisions of the special condition remained operative, the purchaser was not in default and therefore there could be no valid termination by the vendor.

The Court went on to hold (even though it was not strictly necessary) that even if the right to rescind was not available for exercise because of the expiry of the seven day period, the true position was that the contract continued in operation in its conditional state. As both parties had sought to rescind (even if their attempts had been ineffective), the parties had evidenced an intention of the contract no longer being in force even though neither of them was in default, and therefore the contract effectively became abandoned.

This decision highlights the necessity of carefully drafting conditions, and observing all of the timeframes not only in special conditions but also in the standard clauses of the contract for sale.

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