PALLETT VALO LLP
Lawyers & Trade-Mark Agents

Your Authority For:
Business Law • Commercial Litigation • Commercial Real Estate
Construction • Insolvency & Corporate Restructuring
Employment & Labour • Wills, Estates & Trusts

www.pallettvalo.com

Commercial Real Estate

March 2015

The Essentials of the Agreement of Purchase and Sale

A properly drafted and executed agreement is particularly important in real estate transactions. Without it, the entire basis for the transaction may be void. Ultimately, every lawsuit pertaining to the transfer of property between a purchaser and vendor involves the careful consideration of the Agreement of Purchase and Sale which gave rise to the particular rights between the parties. Very few provisions are deemed to be included in an Agreement of Purchase and Sale by statute. For solicitors, commenting upon or drafting this important contract represents not only the opportunity to provide the highest value legal services to a client, it also represents the last and only real opportunity for a lawyer to avoid a "problem transaction."

There are hundreds of precedents and pre-printed forms of Agreements of Purchase and Sale in use today. This is perhaps not surprising, given that each transaction involves the need to set out particular protections, entitlements or rights which one or both parties wish to reduce to writing to enable them to be enforceable in accordance with the "business deal" which the clients have formulated between or among themselves. Great care must be taken by solicitors to consider, in each case, how these provisions apply to the task of representing the interests of a particular client in a particular transaction. Certainly, this high standard will be imposed by a Court when a party to a written agreement argues that it should be excused from strict compliance with an obligation imposed on it in writing.

Below is a list, although not exhaustive, of a number of the salient provisions that represent "hot button" matters which clients should discuss with their solicitor when an offer is being prepared or reviewed.

The Parties and the Property

Who is the purchaser? In many cases, the purchaser has not fully considered who should own the property which is being purchased and who should be burdened with the obligations of the agreement. This is not a simple matter. For example, if a purchaser intends to purchase property from which it will run its business, a purchaser will need to consider whether it really wants to put its operating company – with all of its assets, retained earnings, and representing, perhaps, a lifetime of work – as registered owner of the property on closing and to be directly responsible to the vendor under the Agreement of Purchase and Sale. It may make more sense for a purchaser to incorporate an entity which will own only the property, and lease the property to the operating company, for a host of reasons relating to liability avoidance and possibly for income tax efficiency considerations. Such an arrangement will help to better protect the purchaser in the event that the transaction results in a claim against the purchaser for failing to complete the transaction for reasons which do not appear to the vendor as being legitimate.

In addition, it will be important to ensure that the parties are legal entities. Parties such as "The ABC Club," "The National BCE Association," "The GHI Company" and "Widgets 'R' Us" are, at most, unincorporated associations or, possibly business styles, but do not appear to be valid legal entities (such as individuals or corporations). These issues become very important if a matter proceeds to litigation, as the parties must be properly described in order to ensure that (1) the judgment is enforceable at the end of the process; (2) a plaintiff has legal standing to make the claim in the first place; and (3) parties are not taking on personal liability where they believed another entity (i.e. the non-legal entity that was party to the agreement) was liable.

Finally, in respect of the parties, it is important to discuss with your lawyer the effect of dealing with a party who has entered into the agreement "in trust," "in trust for a corporation to be incorporated," and "in trust for John Smith, and without personal liability." The entitlement or liability of a party, whether as plaintiff or as defendant, may be substantially different, depending on how they are described in the Agreement of Purchase and Sale.

The property must also be properly described. Where the land is not described in accordance with a registrable legal description, it may be necessary to depict the property,

including the boundaries, with appropriate dimensions, as a Schedule to the Agreement of Purchase and Sale. Care must be taken to do so accurately, because where the property cannot be readily identified from the Agreement of Purchase and Sale, it may be impossible to enforce the contract. In addition, property which is not adequately and accurately described can create a nightmare for the purchaser's solicitor when it comes time to search the property to ensure that the purchaser will obtain good title. If the land is situated in a jurisdiction in which it is possible to search title electronically, it is well worth the few minutes and likely minor cost for your lawyer to double-check the legal description which, on occasion, has been provided by a real estate agent or one of the parties at a time prior to the execution of the Agreement of Purchase and Sale.

Finally, it may be useful for a vendor to use the same lawyer in preparing the Agreement of Purchase and Sale who acted for the vendor when it purchased the property, perhaps several years ago. The lawyer may be aware of title or other issues which could be adequately addressed in the draft agreement thereby avoiding arguments and issues after its execution, which on occasion lead to deals not being completed or submitted for a determination by the courts as to the reason for the failure to complete the transaction.

If possible, it is sometimes very useful for a party's solicitor to attend at the property to view it. This applies to solicitors acting for either the vendor or the purchaser. The trained eye of a lawyer can sometimes disclose apparent possessory title issues, potential prescriptive easement issues, encroachments, and the existence of easements, both registered and unregistered, which could not be discerned from a review of title documents from the solicitor's office.

Bu$ine$$ I$$ue$

A solicitor will not usually give advice as to the reasonableness of a proposed purchase price or the sufficiency of the deposit, as this would not normally constitute legal advice, although sometimes a lawyer acting for a purchaser or a lender will see that the property has changed hands many times over a short period, which could be an indicator of value fraud. However, to whom the deposit is paid and how it is held is an important question which you should raise with your solicitor. It is customary that a deposit, for example, is not paid directly to the vendor, but is held in trust either by the vendor's solicitors or by the listing agent (or less typically by the purchaser's solicitor). It is unlikely that, even in the face of a clear breach by a defaulting party, the person holding the monies will release it to the non-defaulting party without obtaining a release duly signed by the defaulting party. In my experience, this often comes as a surprise, both to the purchaser and the vendor.

Where the deposit is large, or the closing is several weeks or months away, it is necessary to address what is to be done with the deposit. Typically, the holder of the deposit is required to place it in an interest bearing account. The party to whom any interest is paid (usually the purchaser upon successful completion of the transaction or the vendor in the event the deposit is forfeited) will need to report such interest in its tax return.

It is important for a lawyer to know how a client proposes to pay for the purchase of the property as it will directly affect the amount of work involved and the requirements that may have to be met for closing. The purchase price may be made up by a cash payment from the client's own resources, a private mortgage from family members, a mortgage from a Schedule 1 bank, a mortgage from a client's or some other person's RRSP, a vendor take-back mortgage, etc., or any combination of the foregoing. Each of these will require significant revisions or additions to many standard Agreements of Purchase and Sale, and financing will raise a host of issues to be negotiated between the parties and a lender. One size will not fit all for these methods of financing the transaction. They will also have a very direct impact on the amount of time your lawyer can expect to spend on the file and, therefore, will also directly affect the amount of fees to be incurred in the transaction.

Harmonized Sales Tax is also an important issue which must be addressed in the Agreement of Purchase and Sale. It is not wise to rely on the provisions of the standard form agreement as the required provision will vary substantially, based on the nature of the transaction.

Finally, it will be necessary for you to discuss with your lawyer any method for the calculation of the purchase price to ensure that it makes sense, is workable, and is in accordance with your understanding of the business arrangement between you and the other party to the transaction. For development property, difficulties sometimes arise when the Agreement of Purchase and Sale contains a description of various portions of the property which are not to be included in the formula for calculating the purchase price where the purchase price is determined by a per-acre amount. Careful drafting is required, as a number of "non-legal" business terms are sometimes not clearly understood by both parties and are difficult to apply (such as “hazard lands” and “lands below top-of-bank”) later when issues arise. Many of these terms have no precise legal meaning and must be defined in order to avoid disputes later.

Timeframes

It will be necessary in most instances to consider the appropriateness of various timeframes for the achievement of certain stages or due diligence in the purchase. For example, it is usual that an offer prepared by a purchaser will contain the shortest possible irrevocable date, to encourage the vendor to accept the offer or to provide a counter offer, and not to “shop” the offer to other parties who may be interested. The title search date, also known as a requisition date, should allow a purchaser's lawyer enough time to be able to complete the search of title and other non-title related enquiries (such as tax arrears, condominium common expense arrears and a municipal work order inquiry, among others). Sometimes, municipalities will take several weeks to respond to enquiry letters. Some government agencies and Ministries take even longer. In discussing the necessary timeframes with your lawyer, it would also be a good time to examine the possibility of using title insurance to solve title problems or to reduce the extent of your lawyer's legal due diligence enquiries.

It is generally unwise to sign an Agreement of Purchase and Sale prepared by a real estate agent, the other party, or the other party's lawyer, without obtaining your own lawyer's advice prior to signing. After execution, it is often not possible to insist on any amendments to the agreement and the parties are usually completely bound by the written agreement (even if it doesn’t truly reflect the bargain the parties made) unless both parties are in agreement to making changes. Certainly, if the transaction starts to become acrimonious, it will be very difficult to amend any provision because the parties are usually jockeying for the best possible “high ground” on the legal battlefield.

Title Clauses

Far too little effort is put into reviewing title clauses, both on standard form agreements and in freely drafted agreements. A clause which obligates a purchaser to accept title subject to “municipal utility easements” may be satisfactory to a residential purchaser who never intends to construct a pool in the backyard, but a purchaser acquiring land for development will not want its development impacted as a result of, for example, a municipal easement for utilities which effectively ends the plan for a new building or expansion of an existing facility. It is very important to discuss with a lawyer the particular purposes for which the property is being acquired in the course of negotiating the title clause, and it is equally important for a vendor to understand its obligations to obtain severance of the property where required, to remove title defects and to otherwise exercise its best efforts to satisfy a purchase’s valid requisition. All of these matters will be addressed, in some fashion, in the title clause.

Bear in mind also that there is a “silent third party” in most Agreements of Purchase and Sale. A lender has its own requirements for clear title which may not accord with the purchaser’s concerns. For example, the purchaser may be prepared to accept title subject to a third party option to purchase (because the purchaser is satisfied that it can comply with the pre-conditions to the exercise of the option to purchase), but the bank may not be prepared to have its mortgage subject to it. Obviously, in these circumstances, the vendor will look to the purchaser to comply with its obligations to complete the transaction (where there is no condition respecting financing or where it has already been waived), so the purchaser sometimes finds itself in a very difficult situation with a looming closing date and no money.

The "Fine Print"

One of the most difficult matters for a party to overcome is one which depends on the argument that an exhaustive and carefully worded clause, which is particular in its application, and which is included in the contract for the sale and purchase of real property, should be disregarded because it was included by one party by inadvertence. A careful purchaser and vendor take the time to review with their lawyers all provisions in the Agreement of Purchase and Sale regardless of their font size, and to modify or delete them where they are not appropriate for the particular transaction.

Conclusion

A client who proceeds without obtaining legal advice prior to signing a binding Agreement of Purchase and Sale may discover that the only function that his lawyer can later play is to deliver the unhappy advice in a transaction which has become acrimonious and confrontational that there is little relief in view of the provisions of the contract to which his or her client has bound itself. The extent of the necessary advice will depend on the type of transaction, the sophistication of the client, and various other matters, only some of which are addressed above.

This paper was originally prepared for and published in the Canadian Bar Association National Real Property Section Newsletter in November 2013.

Ray Mikkola is a Partner in the Commercial Real Estate Practice.

Pallett Valo LLP Commercial Real Estate Practice

We have experience in all areas of Real Estate Law, from the most complex joint ventures and land development projects to routine commercial purchase, sale and mortgage transactions. We assist our clients as they structure and negotiate their projects, and we strive to creatively and effectively overcome any obstacles which arise during the course of a transaction. Our "outside the legal box" thinking and practical, business approach allows us to best serve and protect our clients.

Areas of Practice Include:

- Commercial and Residential Land Development
- Construction Contracts
- Rezoning and Minor Variance Applications
- Condominium Development
- Severance Applications
- Commercial Transactions
- Leasing
- Builder Sales
- Joint Ventures
- Mortgage Financing

Contact Members of our Commercial Real Estate Practice

Murray Box mbox@pallettvalo.com
Direct Dial: 905.273.3022 Ext. 240

Pamela Green pgreen@pallettvalo.com
Direct Dial: 905.273.3022 Ext. 265

Steven Pordage spordage@pallettvalo.com
Direct Dial: 905.273.3022 Ext. 286

Andréa Brinston abrinston@pallettvalo.com
Direct Dial: 905.273.3022 Ext. 219

Ray Mikkola rmikkola@pallettvalo.com
Direct Dial: 905.273.3022 Ext. 276