

CONVEYANCING

Returning to deposits...

Can a failed purchaser recover their deposit if the vendor subsequently sells the property at a higher price?

Mark Pawlowski examines a recent Court of Appeal ruling



Mark Pawlowski is a barrister and professor of property law in the department of law at the University of Greenwich

'The crucial point was that a deposit was an earnest for the performance of the contract and, consequently, could be retained by the vendor on the purchaser's default regardless of whether the vendor had suffered any actual loss as a result of non-completion of the sale or the amount of the deposit.'

In an article earlier this year ('Return of deposits', *PLJ209*, 28 April 2008, p18) I ventured to suggest that an increase in market value would not, on its own, justify the return of a purchaser's deposit under s49(2) of the Law of Property Act 1925. At best, this was merely a factor that had to be weighed against the need for certainty in transactions for the sale of land where the clear expectation of the parties was that a deposit would be retained by the vendor if the purchaser failed to complete the sale.

Most recently, the Court of Appeal in *Midill (97PL) Ltd v Park Lane Estates Ltd & anr* [2008] has affirmed the view of the trial judge, HHJ Mackie QC, that, in order for the Court to exercise its discretion under s49(2) to order the repayment of a deposit, there needed to be something special or exceptional to justify overriding the ordinary contractual expectations of the parties that the purchaser would lose its deposit if it defaulted.

The facts

Gomba International Investments Ltd (Gomba) owned a company (Park Lane Estates Ltd) whose only asset was a commercial property in Park Lane, London. The claimant (Midill (97PL) Ltd) entered into a contract with Gomba to buy the company. The contract provided for the payment of a 10% deposit when the contract was signed, a further payment later on, and the balance on completion.

The claimant made the interim payments but failed to complete the purchase. Gomba then sought to rescind the contract and later sold the company to a third party for a higher price than that originally agreed with the claimant. One of the issues in dispute between the parties was whether the Court should exercise its discretion under s49(2) and

order Gomba to repay the deposit. The claimant argued that the resale of the property for a profit amounted to a special circumstance to justify the return of the deposit. Gomba, on the other hand, submitted that it was entitled to keep the deposit irrespective of the profit it had made on resale.

First-instance decision

Although, strictly speaking, the transaction was a contract for the sale of shares in a company (and not land), it was conceded by Gomba that the share sale fell within s49(2) as being 'a contract for the sale or exchange of any interest in land'.

Having disposed of this preliminary point, HHJ Mackie QC held that Gomba was entitled to keep the deposit despite the fact that it had resold the property for a higher price. Applying the guidance given by Arden LJ in *Omar v El Wakil* [2001], the starting point was that a deposit was an earnest for performance and therefore should not normally be ordered to be repaid unless the circumstances for exercising the Court's discretion under s49(2) were exceptional. Even if the vendor had obtained a profit on resale, this was only a factor to be considered as part of all the circumstances and was by no means conclusive. In the words of the learned judge (at para 32):

If the position were otherwise and the liability to repay the deposit depended upon some future sale price, there would be considerable uncertainty possible for a lengthy period. That would create precisely the uncertainty which a fixed deposit is intended to avoid.

In the instant case, according to the judge, there was no special factor that justified departing from the normal rule. The

claimant was a 'sophisticated investor' that was fully aware of the risks involved in failing to complete the sale.

Court of Appeal ruling

Carnwath LJ (with whom May and Keene LJJ agreed) found no difficulty in upholding the approach taken by the trial judge. In particular, it was apparent from the authorities that there needed to be something special or exceptional to justify overriding the normal rule that a deposit would become forfeited on the purchaser's default.

(a) Weight of authority

In *Michael Richards Properties Ltd v St Saviour's Parish, Southwark* [1975] Goff J, in refusing to order the return of the deposit, concluded that the jurisdiction under s49(2) should only be exercised 'sparingly and with caution'. Similarly, in *Cole v Rose* [1978] HHJ Mervyn Davies QC opined that an order under s49(2) would only be appropriate if there were 'some special circumstances' in the case, being circumstances that suggested that it would be unfair or inequitable that the purchaser should lose its deposit. More significantly, in *Bidaisee v Sampath* [1995], a case involving the return of a deposit under an identically worded provision in a Trinidad and Tobago statute, the Privy Council concluded that the absence of any loss by the vendor (because it had resold at a profit) did not of itself provide a sufficient reason for the Court to exercise its discretion in favour of a defaulting purchaser. In the words of Lord Nicholls:

The traditional deposit paid by a buyer when he enters into a contract is an earnest for the performance of the contract, and can be retained by the seller if the buyer defaults. Equity does not regard this as a penalty against which it granted relief... Section 49(2) has never been understood as intended to overrule that principle, and it should not be so interpreted or applied.

Thus, according to his Lordship, there had to be 'something more' to justify the Court's intervention. In that case, the vendor's profit in reselling the land at a higher price was largely offset by the amount of interest that the vendor would have received had the sale been completed on time. In addition, the Court was not made aware of the reason for the higher price. The enhanced price could have been due to movements in land

prices generally, as opposed to the vendor obtaining a particularly good price for the specific land in question. Because this was a matter of speculation, it did not, according to Lord Nicholls, form a proper basis upon which the Court could exercise its discretion.

More recent cases have adopted a similar approach. In *Omar*, referred to

This approach was followed most recently in *Aribisala v St James' Homes (Governors Dock) Ltd* [2008] (which formed the subject of my earlier article, mentioned above), in which Floyd J concluded, *inter alia*, that although the vendor's profit on resale (amounting to £366,000) was a factor to be taken into account, it was not decisive and certainly

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above, Arden LJ expressed the view that, in the context of a conveyancing transaction, it was common knowledge that if a purchaser failed to complete, it was likely to lose its deposit and so, it was important that there should be certainty attaching to the consequences of paying a deposit. In her view, the circumstances had to be 'exceptional' in order to make it appropriate for the Court to exercise its discretion under s49(2).

not enough (by itself) to make the situation different from the ordinary case where a deposit was not refundable. As a factor to be taken into account, a profit on resale could be significant in appropriate circumstances, but only in assessing 'the overall economic impact' on the vendor in the purchaser failing to complete. In *Tennaro Ltd v Majorarch Ltd* [2003], for example, Neuberger J took into account the fact that the vendor

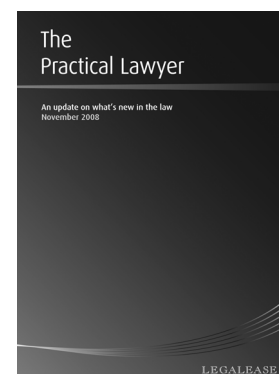
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Section 49(2) of the Law of Property Act 1925: a reminder

In the context of a contract for the sale of land, a seller's right at law to forfeit the purchaser's deposit is mitigated by s49(2) of the Law of Property Act 1925, which gives the courts a wide discretionary power to order the repayment of any deposit 'if it thinks fit', dependent on a general consideration of the conduct of both parties (especially the purchaser), the gravity of the matters in question and the amount at stake (*Schindler v Pigault* [1975] and *Universal Corporation v Five Ways Properties Ltd* [1979]). Although the jurisdiction is statutory, nevertheless, its discretionary character has been held to be at least akin to equitable relief against forfeiture (*Schindler*, above, at 336, per Megarry J) The subsection provides:

'Where the court refuses to grant specific performance of a contract, or in any action for the return of a deposit, the court may, if it thinks fit, order the repayment of any deposit.'

While any limitation or restriction on the scope of the courts' discretion under s49(2) would appear to be inappropriate in view of the broad wording of the subsection itself, it is apparent that a number of guidelines have emerged from cases as to the circumstances in which the discretion to relieve from forfeiture should be exercised in favour of a purchaser.

could have sold the property at a higher price but declined to do so without giving any proper explanation for the refusal. Significantly, the purchaser itself had found the new purchaser (which was willing to pay more than the contract price) prior to the completion date. The decision, therefore, to exercise the discretion under s49(2) turned very much on special facts.

(b) Wider view

Against the more restrictive approach apparent in *Omar* lies the view taken by Buckley LJ in *Universal Corporation v Five Ways Properties Ltd* [1979], who opined that the Court had an unqualified discretion under s49(2) to order repayment of a deposit when this would represent the 'fairest course between the parties', subject only to the discretion being exercised judicially and with due regard to all the relevant circumstances.

This wide interpretation of the subsection has been followed in some cases (notably, *Dimsdale Developments (South East) Ltd v De Haan* [1984], albeit with some reluctance) and has found support amongst several academic writers (see Jones and Goodhart, *Specific Performance* (2nd ed), p304-305, Treitel, *The Law of Contract* (12th ed), p1084-1086 and Goff and Jones, *The Law of Restitution* (7th ed), para 20-035) who have felt that there is no need to unduly restrict the court's discretion by reading into the subsection additional hurdles or requirements. In this connection, the wording of s49(2) expressly provided for an unfettered discretion entitling the court to order the repayment of a deposit 'if it thinks fit' to do so.

(c) Balance of judicial view

Despite the academic support for the so-called 'wider view' expressed by Buckley LJ in *Universal Corporation*, the

Court of Appeal in *Midill* felt bound to adopt the 'most recent, considered guidance' provided by Arden LJ in *Omar*, which clearly had the benefit of being in line with the balance of judicial opinion, including, most notably, the Privy Council in *Bidaisee*, referred to above.

The crucial point, therefore, was that a deposit was an earnest for the performance of the contract and, consequently, could be retained by the vendor on the purchaser's default regardless of whether the vendor had suffered any actual loss as a result of non-completion of the sale or the amount of the deposit. Essentially, in the words of Lord Nicholls in *Bidaisee*, there had to be 'something more', or (as expressed by other judges) 'something special or exceptional', to justify the Court's intervention under s49(2).

Conclusion

The question, of course, remains as to what will constitute 'something more' in the given circumstances of a particular case. Interestingly, the Court of Appeal did not doubt the correctness of Neuberger J's decision in *Tennaro*, mentioned above, as being a special case where the facts were highly unusual given the very attractive (alternative)

offer made to the vendor before the time of completion (which had been arranged by the purchaser itself) and the lack of any stated reason by the vendor for rejecting it. By contrast, however, on the facts in *Midill* it was clearly not enough that the vendor had sold at a higher price some months after the date for completion. The delay in reselling distinguished the case from *Tennaro* but, more importantly, there was nothing to indicate that the resale price was exceptional, given movements in the market generally. In the words of Carnwath LJ:

... there is no obvious reason why the purchaser should have the benefit of any such price rise... it was the vendor who had borne the risk and cost of holding the property during the intervening period.

It seems, therefore, that the mere fact that prices have increased in a rising market will not be enough to persuade a court to order the repayment of the deposit. However, the position may be very different if the vendor has been given the opportunity (by the purchaser) prior to the completion date to sell to another purchaser who is willing to pay more than the contract price. ■

Aribisala v St James' Homes (Governors Dock) Ltd
[2008] EWHC 456 (Ch)

Bidaisee v Sampath
[1995] NPC 59

Cole v Rose
[1978] 3 All ER 1121

Dimsdale Developments (South East) Ltd v De Haan
(1984) 47 P & CR 1

Michael Richards Properties Ltd v St Saviour's Parish, Southwark
[1975] 3 All ER 416

Midill (97PL) Ltd v Park Lane Estates Ltd & anr
[2008] EWHC 18 (Ch);
[2008] EWCA Civ 1227

Omar v El Wakil
[2001] EWCA Civ 1090

Schindler v Pigault
(1975) 30 P & CR 328

Tennaro Ltd v Majorarch Ltd
[2003] EWHC 2601 (Ch)

Universal Corporation v Five Ways Properties Ltd
[1979] 1 All ER 552