

Are Deposits Recoverable by a Purchaser when a Property Transaction is Aborted?

In a typical property sale and purchase transaction, one of the following two scenarios may take place leading to the formation of the contract between the parties:

Option to Purchase

1. The owner of a property grants to a potential Purchaser an exclusive option to purchase ("OTP") the property at an agreed price ("Purchase Price") upon the Purchaser paying an Option Fee of 1% of the Purchase Price.
2. The OTP expires at the end of a specified period (usually two weeks). If the OTP is not exercised within this period, it lapses and the Vendor property owner retains the Option Fee.
3. The Purchaser may exercise the OTP within the validity period by paying an additional sum (most often 4% of the Purchase Price) to the Vendor.
4. This sum, together with the Option Fee, forms a "Deposit", which is also part-payment of the Purchase Price.
5. At this point, a binding contract for the sale & purchase of the property is formed, with completion usually scheduled to take place within 8 to 12 weeks.

Sale & Purchase Agreement

1. In this scenario, the Vendor, instead of granting an OTP, immediately enters into a Sale & Purchase Agreement ("SPA") with the Purchaser.
2. As part of the contractual terms upon signing the SPA, the Purchaser pays a "Deposit" of usually 5-10% of the Purchase Price of the property to the Vendor. Just like in the OTP scenario, this Deposit forms part-payment of the Purchase Price.

Is a Deposit recoverable?

If a Purchaser subsequently defaults on his obligations under the OTP or SPA, and decides not to complete the purchase of the property,

the Vendor has a variety of remedies available to him under both existing contractual rights and the common law.

It should be noted that most OTPs and SPAs are silent as to what happens to the "Deposit" should the contract be repudiated by the Purchaser¹.

The main focus of this article will be on whether the "Deposit" paid is recoverable by the Purchaser in the event the contract is terminated due to his default.

Law Society's Conditions of Sale

Even though the main contract may be silent on this matter, most OTPs and SPAs will incorporate by reference the Law Society's Conditions of Sale 2012 ("Conditions of Sale") – a set of terms and conditions meant to facilitate property transactions.

Condition 15 of the Conditions of Sale is titled "Notice to Complete"². Under this Condition, there is a sub-Condition which states that "without prejudice to any other rights or remedies available to him at law or in equity, the Vendor may forfeit and keep any deposit paid by the Purchaser".

This is after the Purchaser defaults on his obligation to complete the transaction on the scheduled date, and then further fails to comply with a Notice to Complete issued by the Vendor.

Nevertheless, it is possible to contract out of any or all of the Conditions of Sale, even if they have been incorporated by reference. Condition 16 specifically provides that "any special conditions agreed to under a contract [...] shall prevail" if there is any conflict between

¹ It should be made clear that we are referring to a situation where the Purchaser defaults on his obligation to purchase the property without any good reason as provided for under the terms of the contract.

² For OTPs or SPAs which incorporate the Law Society's Conditions of Sale 1999 instead, there is a materially similar Condition in the older version as well.

those special conditions and the Conditions of Sale.

Therefore, if the OTP or SPA itself stipulates that, in the event of termination, any monies already paid shall always be recoverable, this would override the Conditions of Sale even if they had been incorporated.

Nature of a "Deposit"

We have looked at the interaction between the Conditions of Sale (should they apply) and any contractual provisions. But what if the OTP or SPA is completely silent on the matter and the Conditions of Sale have not been incorporated into the contract or have been excluded? In the absence of express contractual provisions, is the Deposit recoverable under common law?

Generally, when a sum of money (in this case, the "Deposit") is paid pursuant to a contract, it can have one or both of the following characteristics:

- (a) it is meant to be advance or part-payment of the consideration.
- (b) it is meant to be "earnest money"; a sort of "guarantee" from the payer to the payee that the former will fulfill his obligations under the contract.

In *Lee Chee Wei v Tan Hor Peow Victor*³, the Singapore Court of Appeal stated unequivocally that if the sum paid is merely meant to be either an advance or part payment, it will be recoverable by the payer in the event that the contract is terminated on his default.

On the other hand, if the sum paid (regardless of whether it is meant to be part-payment) has characteristic (b), it will not be recoverable.

Whether a sum paid has characteristic (b) ultimately depends on the construction of the contract, and on the intention of the parties.

In the situation we are concerned with, the sum of money paid pursuant to the exercise of an OTP or to entering into an SPA is usually labeled as a "Deposit". This is a strong indication that the parties to the contract intended for it to have characteristic (b).

Accordingly, under common law, if a Purchaser breaches his obligation to purchase the property in an ordinary sale and purchase situation, the Vendor is very likely entitled to retain the Deposit, in addition to claiming for any damages suffered as a result of the Purchaser's default.

Pre-contractual "Deposit"?

In *United Artists Singapore Theatres Pte Ltd and another v Parkway Properties Pte Ltd and another*⁴, Belinda Ang J made a distinction between:

- (a) "deposits" paid pursuant to a contract; and
- (b) "deposits" paid prior to formation of a contract.

So far our discussion has involved the normal exercising of OTPs and entering into of SPAs where any deposit is clearly paid pursuant to the formation of a contract.

Sometimes, however, when parties are in discussions "subject to contract", monies may well be paid in anticipation of an agreement.

In such cases, regardless of whether the sums are labeled as a "deposit" or not, they will always be recoverable should the parties subsequently fail to formalize the contract.

Penalty Clauses and Forfeitable Deposits

In Singapore, the usual amount of deposit paid pursuant to OTPs or SPAs is 5% (or sometimes 10%) of the purchase price of the property.

An interesting question arises if the "deposit" paid under the contract is more than 10% of the purchase price. What if the deposit is, say, 50% of the purchase price?

If the Purchaser subsequently defaults, should the Vendor be entitled to keep the 50%? Would that be excessive? If so, where should the line be drawn?

Although such questions have yet to be answered definitively by the Singapore Courts, in *Triangle Auto Pte Ltd v Zheng Zi Construction Pte Ltd*⁵, Selvam J made it clear that "if the deposit amount is excessive it will also be caught by the law of penalty"⁶. A forfeitable deposit of 10% has always been regarded by the court as reasonable, but if the Vendor wishes to forfeit any higher amount of deposit, the burden will be on him to prove its reasonableness.

³ [2007] SGCA 22 at paragraphs 84-85.

⁴ [2002] SGHC 185

⁵ [2000] SGHC 229.

⁶ *Ibid* at para. 12.

Conclusion

When a Purchaser enters into a contract for the purchase of immovable property, he may wish to protect himself from the forfeiture of any deposit paid by expressly inserting a clause allowing for refund, or by characterizing any payment made as an advance or part-payment and not as a deposit.

On the other hand, a Vendor is, by default, entitled to forfeit a Purchaser's reasonable deposit under both common law and the Conditions of Sale and should be aware of any attempt by the Purchaser to deviate from the two.

Ultimately, the insertion of any specific contractual term will always depend on the relative bargaining strength of the parties and the importance they attach to the terms.

If you wish to have further information on this update or wish to discuss how it may potentially have an impact on your business, please feel free to contact the following:



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