CITATION: Konialian v. Paletta, 2020 ONSC 3976
COURT FILE NO.: CV-19-2373 and CV -19-1809
DATE: 20200626

ONTARIO

SUPERIOR COURT OF JUSTICE

BETWEEN:	)	
	)	
RAFFI KONIALIAN AND TAMARA KONIALIAN,	)	Paul Le Vay and Emily Quail, for Raffi Konialian and Tamara Konialian
Applicants/Respondents on Cross-Application	)	
– and –	)	
	)	
MICHAEL JOSEPH PALETTA and PALETTA INTERNATIONAL CORPORATION,	)	Frank J. Sperduti and Andrew Baker, for Michael Joseph Paletta and Paletta International Corporation
Respondents/Applicants on Cross-Application	)	
	)	
	)	**HEARD:** January 20, 2020

REASONS FOR JUDGMENT

CHOZIK J.

A. OVERVIEW:

[1] This is an application by Raffi and Tamara Konialian (the "Konialians") for a declaration that a repurchase and daily penalty provision under an Option Agreement is unenforceable and for relief from forfeiture under section 98 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43. Michael Paletta ("Michael") and Paletta International Corporation ("Paletta International") bring a cross-application to enforcement the Option Agreement

in question. These applications proceeded before me on affidavits and transcripts of cross-examinations of Michael, Raffi Konialian ("Raffi"), and Angelo Paletta ("Angelo").

[2] The central issue in this case is whether or not the forfeiture and penalty provisions in an Option Agreement attached to the agreement of purchase and sale between Michael and Raffi for the purchase of a vacant lot in a subdivision (the "APS") are enforceable. These provisions required the purchaser, Raffi, to sell the property back to the vendor, Michael, for 25 per cent of the purchase price if Raffi failed to abide by certain development requirements. In addition, the Option Agreement allowed Michael to claim, on demand, a daily penalty of $1,000 for any delay in meeting the deadlines for those development requirements.

[3] The effect of these terms is to allow Michael to retain the property and 75 per cent of the purchase price *plus* approximately $270,000 in daily penalties, all in the absence of any evidence that Michael suffered or reasonably anticipated any damages.

[4] For the Reasons that follow, I have concluded that the repurchase and daily penalty provisions of the Option Agreement are unconscionable and should not be enforced. I therefore, exercise my discretion under s. 98 of the *Courts of Justice Act*, to grant the Konialians' relief from forfeiture.

[5] If I am incorrect in regard to the enforceability of those provisions, I also find that Michael waived his rights under the Option Agreement to enforce compliance with the construction schedule. He did so through the conduct of his agent, Angelo**.**

B. BACKGROUND:

[6] The "Bluffs of Burlington" ("the Bluffs") is a luxury rural estate residential subdivision developed by Paletta International. The first phase of the Bluffs was registered in 2003. A second phase was registered in 2006. The subdivision contained 34 lots, 29 of which were sold to third-party purchasers. Each lot is at least two acres and

located in a secluded wooded area. Four lots, including Lot 12, were owned individually by members of the Paletta family.

[7] Michael is Paletta International's Vice-President. His brother, Angelo is the President and CEO. Michael purchased Lot 12 from Paletta International in 2010 for $75,000 (which was materially less than market value at the time). In December 2016, Raffi[1] bought Lot 12 from Michael for $1,050,000, plus HST. He and his wife, Tamara, intended to build their dream home there.

Terms of the APS

[8] Although the Konialians bought the lot from Michael personally, and not from Paletta International, the terms of the APS were subject to standard form agreements created by Paletta International. These standard form agreements were used for all of the sales of lots in the Bluffs, except those sold to members of the Paletta family. Those Paletta International standard form agreements included an agreement of purchase and sale form, a schedule "D" to that agreement, and an option agreement.

[9] On December 20, 2016, Michael and Raffi entered into the APS based on the Paletta International standard form agreement. Raffi paid a deposit of $157,500. The closing was set for February 22, 2017.

[10] The terms of the APS required Raffi to: (a) build a custom home of at least 5,000 square feet; (b) submit architectural drawings for approval by Michael; (c) use a builder chosen by Michael; and, (d) comply with a construction schedule. The Notice provisions in the APS specified that whenever notice was required under the agreement, it was to be provided to Angelo and the lawyer for Paletta International.

[11] The construction schedule was demanding. As set out in sections 10.1 - 10.3 of the APS, Raffi was required to: (a) "commence construction" within six months of closing,

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[1] The initial APS was signed by Raffi, alone. It was later assigned to Tamara Konialian.

and (b) continue with construction as expeditiously as possible and continuously in order to have substantially completed the dwelling unit within 18 months “from the above date.”

[12] The APS did not provide for the possibility of extending the six-month term to “commence construction”. However, the APS required the vendor to extend the 18 months for “substantial completion” if the reasons for the delay of the completion were “acts of God, strikes, or other matters beyond the purchaser’s control” and “a reason other than cost to the Purchaser.” The only approved builder for the subdivision at the time was Robinson Custom Homes Inc.

[13] Schedule “D” of the APS provided that if the purchaser defaulted on his obligations to comply with the construction schedule or use the approved builder, or if he sold, transferred, or conveyed the lot prior to substantially completing the home, the vendor had the right to repurchase the lot for 25 per cent of the original purchase price. Further the vendor would be entitled to a daily penalty of $1,000.

[14] In other words, if the purchaser failed to commence construction (as defined) using Robinson Custom Homes within six months of closing – or failed to substantially complete the home within a further 18 months due to the costs of the construction – the purchaser was obligated to sell the property back to the vendor at a 75 per cent discount from their original purchase price (regardless of the value of the property at the time of that compelled sale). In addition, the purchaser also had to pay a $1,000 per day penalty if demanded by the vendor.

Terms of the Option Agreement

[15] For consideration of $2.00, the Option Agreement was signed on closing and registered on title. The Option Agreement set out the following construction schedule in paragraph 1:

> 1. The Purchaser agrees that the Purchaser shall Commence Construction upon the Property by August 22, 2017 and having commenced construction to continue with such construction as expeditiously as possible and continuously in order to have Substantially Completed the dwelling unit within 18 months from August 22, 2017. Such eighteen (18) month period

> shall be extended for a period of time equal to the time of any delay caused by reason of acts of God, strikes, or any other matter beyond the Purchaser's control and which delay was for a reason other than cost to the Purchaser.
>
> "Commencement of Construction" shall be deemed to have occurred with respect to the Lot when the Purchaser shall have obtained a building permit and shall have excavated the basement and fully completed the foundation and basement with respect to the dwelling unit to be constructed on such Lot. "Substantial Completion" shall be deemed to have occurred with respect to the dwelling unit upon such dwelling unit having been sufficiently completed so as to enable such dwelling unit to be fit for human habitation, and with respect to which 90% of the interior and exterior construction shall have been completed (based upon the value of the work in place of relation to the value of the work to be completed), and rough grading has been completed so as to allow proper drainage of the Lot and any adjacent lands dependent upon the Lot for drainage.

[16] Paragraph 2 of the Option Agreement required the purchaser to use an approved builder.[2] It also stated that the vendor's intention was that only one builder be used by various purchasers to construct dwellings on the lots, but that the vendor was not prohibited from designating any other builder from time to time. The purchaser was required to provide a complete copy of any contract between himself and the builder, if requested to do so in writing by the vendor.

[17] With respect to the penalties for default, paragraph 3 of the Option Agreement stated the following:

> 3. The Purchaser agrees that if the Purchaser defaults in the performance of its obligations in paragraph 1 or 2 of this Agreement, or if the Purchaser shall sell, transfer or convey the Lot prior to the Purchaser having Substantially Completed the dwelling unit thereon in accordance with paragraph 1 above, then in each case, the Vendor shall have the right and option (the "Option") to repurchase the Property (together with all improvements situate thereon) for a purchase price of TWO HUNDRED, SIXTY-TWO THOUSAND FIVE HUNDRED CANADIAN DOLLARS

[2] At the time of closing, in addition to the Option Agreement, a second agreement was signed and registered on title. This second Agreement required the Konialians to construct a building on the land, and to use a builder approved in writing by the vendor to do so. This covenant would run with the land for 10 years. The consideration for this Agreement was $10.00

> ($262,500.00) inclusive of HST (the "Repurchase Price"), and in addition (and whether or not the Vendor exercises the Option) the Purchaser shall pay to the Vendor the sum of ONE THOUSAND CANADIAN DOLLARS ($1,000.00) per day for each and every day that the Purchaser is in default under said paragraphs 1 or 2 of this Agreement. Such amount shall be payable to the Vendor ***on demand***. [Emphasis added.]

[18] Significantly, under both the APS and the Option Agreement, there was no possibility of extending the first six-month period for the "commencement of construction" for events outside of the control of the purchaser. Despite his concerns that the initial six-month timeframe to commence construction was unrealistic, Raffi entered into the agreement to purchase Lot 12. He deposed that he did so because Jay Robinson ("Robinson") had assured him that this deadline would not be enforced so long as he was taking steps to obtain a building permit.

[19] Robinson was summoned to attend for examination as a witness in a pending application under r. 39.03 of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194. He did not attend. Neither party moved to compel his evidence. His non-attendance is a neutral fact in my decision.

Steps to "Commence Construction":

[20] The Konialians did not "commence construction" within six months of closing of the sale. Two years after closing, on February 22, 2019, they did not have a building permit or a signed contract with an approved builder. Construction of their home had not commenced. Despite this, from August 22, 2017 (when the six months deadline for commencing the construction passed) until March 8, 2019 (when Michael gave notice of his intention to repurchase the lot), neither Michael nor Angelo (on their own behalf or for Paletta International) voiced any concern about the delay or the obvious failure to comply with this term of the Option Agreement.

[21] Although construction of the home had not started, the Konialians took significant steps towards that end. I find that throughout the relevant period, they were actively working to build an appropriate home on the lot. On February 6, 2017, prior to closing, Raffi retained Joris Keeren ("Keeren"), an architectural technologist, to design the house

and assist with the permitting process. Raffi worked for several months with Keeren towards an initial design.

[22] On March 31, 2017, Raffi received and approved Keeren's initial design, which included only a floor plan, front elevation and site plan. The home, including the garage, was a bungalow. Its footprint was 1,100 square metres (roughly 8,500 square feet) not including the garages. In June 2017, Raffi retained an interior designer. By August 31, 2017 the final design of the bungalow was completed and Raffi signed off on it.

[23] After Raffi approved the final design, Keeren started to prepare the "working" or "permit" drawings and supporting documentation. This next step, according to Keeren, would normally – and did in this case – take several months. To apply for a building permit, the following were required: a zoning clearance certificate, conservation approval and a grading certificate. A grading plan was prepared by a surveyor. Mechanical drawings were obtained from a mechanical designer. A driveway design was done. The drawings had to be approved by a structural engineer and stamped by a more senior architectural colleague, who had also been retained.

[24] On December 5, 2017, the Konialians applied for a zoning clearance certificate, which required them to submit a complete design drawing and site plan. The zoning clearance certificate was granted on January 16, 2018. On December 14, 2017, they obtained conservation approval. The driveway had to be redesigned at one point to be approved by the City of Burlington. In February 2018, Robinson successfully negotiated on their behalf with the City to waive the requirement for a storm water management system. By February 2018, they were ready to apply for a building permit, using their first design.

The Fire Suppression System:

[25] The *Ontario Building Code* required rural homes with a footprint greater than 600 metres but lacking access to fire hydrants, to provide the same amount of water on site as would be available through a fire hydrant. Keeren was not aware of this requirement

when he was first retained to design the bungalow. He testified that it was an unusual requirement triggered by the large footprint ***and*** the rural location of the home.

[26] According to Keeren, the requirement for a fire suppression system came to light after initial discussions with the City of Burlington in July of 2017. Both Keeren and Raffi testified that Robinson referred Raffi to an engineering company to design the fire suppression system, and "ball-parked" the cost of such a system at $100,000. Many months later, when the system was designed, its formal estimated cost was closer to $400,000. Three large tanks of water would have to be buried underground to hold 415,000 litres of water. Two of the tanks were 52 feet long and 10 feet high. A third tank was three quarters of that size. A panel at the Building Department would have to evaluate the system and approve it.

[27] Another option for the fire suppression system put forward was a sprinkler system, which would cost around $48,000. It required a different water holding system. However, there were no assurances from the City of Burlington that either system would be approved.

[28] In February 2018, Raffi decided that the bungalow design was not practicable. He gave evidence that this was not an easy decision, but it seemed to be the most cost and time efficient. He scrapped the first design and started the process all over to design a two-storey home with a footprint of less than 600 square meters. The costs of the first design, $150,000, were thrown away.

[29] The design phase for the second version of the home took from February to September 24, 2018. Then the "working" drawings of the process commenced. According to Keeren, the requisite certificates were obtained and the Konialians applied for a building permit on March 4, 2019. There were a few minor questions raised by the City, and a minor variance was required for the garage. According to Keeren, the expectation was that a building permit would issue.

[30] Raffi testified that, throughout the process, he was assured by Robinson that Angelo was kept updated as to Raffi's progress. Raffi made the decision to scrap the first

design with this assurance. Keeren confirmed that, at the time when the decision to scrap the first design was made, Raffi told him that he felt assured by Robinson that the six month deadline was no longer a hard deadline and that it would not be enforced against him. In an email to Raffi dated February 25, 2019, Robinson stated that he had been periodically updating Angelo.

Failure to Reach an Agreement with Robinson:

[31] By the end of February, 2019, Raffi and Robinson could not reach agreement on a builder's contract. Robinson's estimate for constructing the home was nearly $2 million more than what Raffi was prepared to pay. His management fee was initially over $400,000. Then, they agreed on $300,000, but they could not agree on payment terms, holdbacks and a termination clause.

[32] Raffi also learned that Robinson was required to pay the value of two per cent of the building contract to Paletta International. This would have required Raffi pay another $50,000[3] to Paletta International, essentially for nothing. Robinson sought to include this "fee" in his contract with Raffi. Raffi was adamant that this fee should be borne by Robinson.

[33] In February, Raffi and Robinson exchanged multiple emails about the terms of the builder's contract. Raffi continued to refuse to pay the two per cent fee to Paletta International. In that context, in an email dated February 25, 2019, Robinson cautioned Raffi about the consequences of delay. According to Raffi, this was the first time Robinson ever did so. In this email, Robinson said: "I was able to secure this lot for you", and "I have been periodically updating Angelo and have been telling him I will be in shortly with complete plans for him to approve". Robinson then goes on to say that if Raffi refused to use him as the builder and there were any further delays in commencing the construction,

[3] Although the actual fee would have been $100,000, Raffi deposed that Robinson proposed to minimize the cost by telling Angelo that the construction of the house was $2.5 million, rather than $5 million.

Angelo could take Raffi to court to repurchase the property for 25 per cent, as Angelo had apparently successfully done to two other purchasers.

Raffi's Communication with Angelo in February and March 2019:

[34] At this point, Raffi had not had any direct communication with Angelo since the closing in February, 2017. Raffi gave evidence that he assumed that, as the approved builder with a contractual relationship with Paletta International, Robinson was keeping Angelo updated. On February 4, 2019 Raffi emailed Angelo directly. In that email, Raffi told Angelo that he would start building as soon as winter was over. The two then exchanged multiple emails, during which Angelo expressed no surprise or concern with the delay in submitting plans for approval or commencing construction.

[35] On February 28, 2019, Raffi emailed Angelo to ask whether he could use a builder other than Robinson to construct his home. He told Angelo that he had not been able to work out the details of a final contract with Robinson, and that he would like to use Rob Russo. By this time Russo was approved as a builder in the subdivision and was building the house next door. Angelo replied: "Raffi, you are free to choose between the 2 [sic] as you wish, and yes, I need to see the plans." In my view, this was the written approval of a builder required under the Option Agreement.

[36] On March 1, 2019, Raffi emailed copies of the drawings and asked whether Angelo needed to see the hard copies. On March 5, 2019, Angelo replied that he needed the hard copies and the samples. On March 6, 2019, Raffi and Angelo exchange emails about dropping off the hard copies of the drawings and the samples. At no point did Angelo raise the development requirements with Raffi. By March 3, 2019, Raffi had engaged Rob Russo for the construction of the home.

[37] On March 8, 2019, Raffi finalized arrangements with Angelo to drop off hard copies of the final building plans, as well as relevant samples of products and colours for approval. To that point, every indication was that there was no issue in proceeding with Russo and the new plans. Later in the day, however, Michael's lawyer notified Raffi by

email that Michael intended to exercise the right to repurchase the property pursuant to the Option Agreement, for 25 per cent of the purchase price.

[38] There had been no communications between Michael and the Konialians since December 20, 2016 (when Raffi met with Michael and Angelo to sign the APS). There had been no direct communication between Raffi and Angelo from the time of closing in February 2017 until February 4, 2019. All of Raffi's communications had been with Robinson. Neither Michael nor Angelo asked Raffi about the reasons for the delay in commencing construction. They had never expressed any concern to him about the pace of development. They never warned him that they were contemplating invoking the penalties in the Option Agreement.

[39] The formal "Notice of Exercise of Option to Purchase" stated that the purchaser had "failed to Commence Construction upon the Property by August 22, 2017 and is therefore in default under paragraph 1 of the Option Agreement".

C. POSITIONS OF THE PARTIES:

[40] The Konialians argue that the portion of the Option Agreement that requires them to sell the property to Michael at a mere 25 per cent of the purchase price (at a loss of more than $750,000) and to pay the $1,000 daily penalty are, in law, unenforceable penalties. In the alternative, they seek relief from forfeiture under s. 98 of the *Courts of Justice Act* because those provisions are unconscionable. In the further alternative, the Konialians seek a declaration that Michael waived any right to enforce those provisions, and/or that he is estopped from doing so in light of Angelo's and Robinson's statements and conduct.

[41] Michael and Paletta International ask this court to declare that the Option Agreement is in full force and effect. They seek an order that the Konialians forthwith

close on the sale back of the property to Michael for 25 per cent of the purchase price and pay approximately $270,000[4] in daily penalties for the delay.

[42] Michael and Paletta International say that the Konialians are in breach of their obligation to construct a home on Lot 12 within the prescribed time period. They argue that the Option Agreement was entered into by two sophisticated parties, with the benefit of legal advice. There was no asymmetry in their bargaining power. Public policy favours enforcement of contractual agreement freely entered into by the parties. The right to repurchase does not constitute an unenforceable penalty. Neither Michael nor any agent acting on his behalf, expressly or implicitly waived or amended any terms of the Option Agreement.

ISSUE ONE: UNCONSCIONABILITY

Threshold Issue: Are the Repurchase and Daily Penalty Provisions of the Option Agreement Unenforceable Penalties or Forfeitures?

[43] Determining whether to enforce penalty clauses or grant relief from forfeiture involves a mix of common law and equity. While the prohibition against enforcing penalty clauses comes from the common law, relief from forfeiture is historically an equitable remedy (*869163 Ontario Ltd. v. Torrey Springs II Associates Ltd. Partnership*, 2005 CanLII 23216, [2005] O.J. No. 2749 (Ont. C.A.), at paras 22-24. subnom. and hereafter referred to as "*Peachtree*").

[44] A penalty is the payment of a sum as a consequence of a breach of contract. The reluctance to enforce penalties at common law arises from the lack of any connection between a penalty and any damages, real or anticipated, that arise from the breach giving rise to the penalty (*Peachtree*, at para. 31).

[45] Forfeiture, on the other hand, is "the loss, by reason of some specific conduct, of a right, property, or money, often held as security or part payment of the obligation being

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[4] Initially, Michael sought payment of the daily penalty of $1,000 per day from August 22, 2017 to November 19, 2019 which totalled $819,000. At the hearing of the applications, Michael amended his request to reflect the daily penalty from February 22, 2019 (the last possible breach day) to November 19, 2019.

enforced under the threat of forfeiture" (*Peachtree*, at para. 22). A forfeiture may have penal consequences as, for example, the right or property forfeited by the defaulting party. It may bear no relation to the loss actually suffered by the innocent party.

[46] In *Peachtree*, Sharpe J.A. observed that courts should avoid classifying contractual clauses as forfeitures or penalties. Rather, they should subsume both terms under the rubric of unconscionability. He reasoned that this approach: (a) allows for a more rational framework for decisions with respect to both forfeitures and penalties; (b) is consistent with the direction taken under the *Courts of Justice Act*, which provides relief from penalty and forfeiture; and (c) supports the policy of upholding freedom of contract, which recognizes the advantages of allowing parties to define for themselves the consequences for breach or non-performance of an agreement (*Peachtree*, at paras. 30-34; see also *Infinity Gold Mining Inc. v. Wega Mining,* 2015 ONSC 607, at para. 69 ("*Infinity Gold*").

[47] Section 98 of the *Courts of Justice Act* provides that "[a] court may grant relief against penalties and forfeitures, on such terms as to compensation or otherwise as are considered just." Relief under s. 98 is an equitable and purely discretionary remedy (*Scicluna v. Solstice Two Limited*, 2018 ONCA 176, at para. 28).

[48] The Ontario Court of Appeal decision in *Redstone Enterprises Ltd. v. Simple Technology Inc*, 2017 ONCA 282, sets out the test for unconscionability. The test is the same, regardless of whether one characterizes the contractual provision as a penalty or forfeiture.

[49] Thus, in my view, it is not necessary for me to determine whether the provisions at issue in this case are technically a penalty or a forfeiture. The central issue is whether paragraph 3 of the Option Agreement is unconscionable as that term is understood in the context of a party seeking relief under s. 98 of the *Courts of Justice Act*.

[50] If I am wrong in this regard, and I must classify these provisions as one or the other, I conclude that the daily penalty provision is an unenforceable penalty while the repurchase provision is a forfeiture. The daily penalty, by its very nature calls for the

payment of $1,000 per day for failing to comply with a term of the contract. There is no evidence of any damages warranting such a payment, actual or anticipated. The payment is required on demand. The demand may be made retroactively, as it was here. The demand may be made without notice of the breach, as it was here. It is a penalty. In my view, it is inequitable and unenforceable. The repurchase provision is a forfeiture because it requires the purchaser to forfeit his property for 25 per cent of its value.

[51] Regardless of whether either is a penalty or a forfeiture, I find both to be unconscionable in the circumstances of this case.

Legal Principles: Unconscionability

[52] To be eligible for relief from penalties and forfeiture under s. 98 of the *Courts of Justice Act*, the purchaser must establish that a two-part test is met:

> **(1)** That the penalty or forfeiture is out of all proportion to the damages suffered (i.e. grossly disproportionate); and
>
> **(2)** That it would be unconscionable for the seller to retain the deposit or money to be paid. (*Redstone*, at para. 15, citing *Stockloser v. Johnson*, [1954] 1 Q.B. 476, [1954] 1 All E.R. 630 (Eng. C.A.) ("*Stockloser*")

[53] In *Redstone*, Lauwers J.A. noted that in some, albeit rare, cases, unconscionability may be established purely on the basis of the gross disproportionality between the damages suffered and the amount forfeited (*Redstone*, at para. 26). Even where there is no gross disproportionality, the court can consider other *indicia* of unconscionably. Lauwers J.A. identified a number of considerations that may point to unconscionability such as inequality of bargaining power, a substantially unfair bargain, the relative sophistication of the parties, the absence of *bona fide* negotiations, the nature of the relationship between the parties, the gravity of the breach and the conduct of the parties (*Redstone*, at paras. 29-30). This is a context-specific analysis.

[54] Ultimately, contractual terms may be set aside only in the clearest circumstances. When the parties turned their minds to the consequences of a breach and agreed what those consequences would be, those terms should generally be enforced.

There are strong policy considerations favouring certainty in contractual relations. Claims of unconscionability must be considered, having in mind their specific commercial context (*Peachtree*, at paras. 32-34). In *Redstone*, Lauwers J.A. emphasized that "the finding of unconscionability must be an exceptional one, strongly compelled on the facts of the case" (at para. 25). The court's discretion to pronounce a forfeiture unconscionable would otherwise create uncertainty and should not be understood as "undefined discretion" (*Redstone*, at para. 24).

Application:

(i) Is the forfeiture of the land/daily penalty grossly disproportionate to any damages?

[55] In my view, the repurchase and the daily penalty provisions under the Option Agreement are grossly disproportionate to any conceivable damages. The forfeiture and daily penalty for the Konialians is more than $1 million, and the loss of the property, whereas on the record before me the damages, actual or anticipated, to Michael (or Paletta International) are zero.

[56] I calculate the amount of the forfeiture and penalty as follows:

a. The value of Lot 12 as of May 2019 was $1.3 million;

b. The Konialians paid $1,050,000 plus HST for the lot;

c. They will receive the repurchase amount of 25 per cent, which is $262,500.00, inclusive of HST;

d. The daily penalty of $270,000; and

e. Their costs thrown away of at least $150,000 for the first design, and the unquantified costs for legal fees for the purchase of the lot, second design building permit applications, etc.[5]

[5] I accept that the lost 'sunk costs' may not be part of the "penalty", but they do form part of the factual matrix that is relevant to the overall consideration of whether the terms are unconscionable.

[57] Conversely, I find that neither Michael nor Paletta International have suffered or will suffer any actual damages from the Konialians' delay in commencing construction.

[58] In my view, the proportionality analysis mandates consideration of Michael's damages and not those of Paletta International. The Option Agreement is an agreement between Michael and the Konialians, not Paletta International. Paletta International and Michael are separate legal entities. There is no evidence of Michael's ownership or legal interest in Paletta International. Based on the evidence, he is a senior employee and an officer of the company. There is no evidence that he has any obligation to Paletta International.

[59] Angelo gave evidence that deposits made by Paletta International to the municipality apply to the development. Those deposits have no nexus to this transaction. Michael has no legal obligation to take into account any of Paletta International's interests in concluding this transaction. There is no evidence of any damages suffered by Michael from the failure of the Konialians to comply with the development requirements. I infer that he suffered none.

[60] Even if I consider damages to Paletta International, I can find no link between the sum of the forfeiture and penalties and any actual or potential damages that it suffered. The quantum of both the forfeiture and the penalty are arbitrary. At his cross-examination, Angelo deposed that the 25 per cent and $1,000 figures were just numbers he came up with in 2003. They were intended to make sure that people who bought lots followed through on their obligations and actually built houses. These numbers were not intended to reflect any damages he expected to suffer.

[61] Since 2003, the purchase price of the lots increased substantially, from roughly $350,000 to $1-1.2 million.[6] No adjustment had been made to the repurchase percentage contained in the standard form agreements. I find that the 25 per cent repurchase

[6] In February 2019, when Raffi inquired about it, Angelo told him Lot 5 was for sale for $1.5 million.

provision and the $1,000 daily penalty are entirely arbitrary and not linked to actual or potential loss to Michael or Paletta International.

[62] Michael and Paletta International argue that the right to repurchase and the daily penalty provisions under the Option Agreement are remedial measures to ensure the appropriate development of the Bluffs. The conditions for the sale of the lots to non-family members required buyers to retain approved builders and to complete construction in a timely manner. This was done in order to maintain architectural control over the subdivision, balance quality and consistency, while at the same time permitting purchasers a large degree of customization in developing their properties. It also helped ensure that purchasers actually built on their lots, rather than speculating and/or leaving unfinished homes that would negatively impact the overall development. It protected the developer from the risk of loss of its front-end costs and security deposits that had been sunk into the project. As such, the construction schedule and the penalties were rationally connected to the overall goals of the development at a market price that reflected those obligations.

[63] I accept that the original intention of the penalty and forfeiture provisions was twofold: to prevent speculators from buying and flipping the lots, as well as to maintain architectural integrity and building quality within the subdivision. These terms were intended to prevent partially completed structures left to linger in the development because purchasers ran out of money to complete the construction. These are legitimate goals in this commercial context.

[64] However, there is no logical connection between the repurchase provision and daily penalty to the risk of loss of front-end costs for the development. These are deposits Paletta International made to the municipality. The deposits are held by the municipality until the subdivision is complete. The construction of Lot 12 was not holding up the completion of the subdivision.

[65] Even if the Konialians had complied with the construction schedule, Paletta International could not recoup its front-end costs and security deposits until the whole

subdivision was completed. As of September 2019, there were at least two unfinished lots, owned by Paletta family members. Those family members are not bound by the development requirements imposed upon the other purchasers. They can develop their lots within their own schedules with a builder of their choice, unhindered by the approval of Paletta International. A third lot was still for sale at the time of this hearing. A fourth lot was held by the City of Burlington.

[66] In other words, the subdivision is still not complete. The failure of the Konialians to complete their build has not prevented Paletta International from recouping its costs and deposits. Their property just sits as one of a number of vacant lots. Michael or Paletta International have suffered no loss and can presently anticipate no loss as a result of the Konialians' failure to commence or complete construction by February 2019.

[67] Paletta International was required to give the Konialians an extension of 18 months to substantially complete construction in almost any circumstance other than cost to the purchaser. The standard Option Agreement provided that Paletta International "shall" grant an extension when requested if the reason for the extension was "acts of God, strikes, or other matters beyond the purchaser's control". The inclusion of this mandatory extension suggests that no genuine concern or actual damages arose from delays in construction. So long as the lot was not "flipped" and the construction not abandoned due to lack of funds, the development objectives were met.

[68] The forfeiture and penalty terms are grossly disproportionate to the harm they were intended to remediate in this case. Given the time, expense and genuine efforts the Konialians invested in finalizing the design and applying for a building permit, there is no question they were not speculators. They had every intention of building their dream home on Lot 12.

[69] Michael and Paletta International argue that, to assess the proportionality of the forfeiture, the costs of constructing the home must be included in the calculation. They rely on an estimate prepared by Robinson that the cost of construction of the home would be in excess of $5 million. They argue that when the construction costs are added to the

cost of the lot, the 25 per cent repurchase price is not so disproportionate. It is a mere 13 per cent of the total expenditure required of Raffi. They rely on a number of cases dealing with deposits and repurchase provisions in support of their position.

[70] I disagree.

[71] First, this is not a deposit case. Those cases involve the right of a vendor to retain a deposit in the event of a breach by the purchaser, where the deposit is made to secure the performance of the contract. Michael did not receive a deposit of $1,050,000 for Lot 12, he received the entire purchase price.

[72] Second, Robinson's estimate of $5.3 million was a builder's proposed budget for the construction. It is what the builder *thinks* the client should or could spend on the project. It is not what the client actually decides or agrees to spend. Raffi's evidence is uncontradicted: he was not prepared to spend that much on building this house. His budget was closer to $3.5 million for construction.

[73] Lastly, whatever the Konialians intended to spend on the construction of their home is not relevant to the unconscionability analysis and the proportionality of the forfeiture. As explained by Denning L.J. in *Stockloser*, above, relief from forfeiture requires two things:

> first, the forfeiture clause must be of a penal nature, in the sense that the sum forfeited must be out of all proportion to the damage; and, secondly, ***it must be unconscionable for the seller to retain the money.*** [Emphasis added]

[74] Thus, the question is not whether Raffi was prepared to spend more, but whether it is unconscionable for Michael to retake the property and retain 75 per cent of the total purchase price, and receive the daily penalty when he has suffered absolutely no loss or damages.

[75] None of the cases relied on by Michael and Paletta International involved a repurchase for 25 per cent of the purchase price of the land. In *Cambridge (City) v.*

Simcoe Fox Developments Ltd., 1993 CarswellOnt 5718, [1993] O.J. No. 2847 (Ont. C.J. Gen. Div.), the repurchase was for 90 percent of the purchase price. In *Jain v. Nepean (City)*, 93 D.L.R. (4th) 641,1992 CarswellOnt 588 (Ont. C.A.), the repurchase was at 80 per cent of the purchase price. Two cases from British Columbia interpreted stricter repurchase clauses, but even in those cases the repurchase was at 42 percent and 36 percent of the present value (see *Kamloops (City) v. Interland Investments Inc*., 1979 CarswellBC 561, 9 B.L.R. 130 (B.C.S.C.), and *Rae et al v. Brooks*, 2003 BCSC 1576). I also note that these decisions are very dated.

[76] In the more recent decision in *Infinity Gold*, a more significant forfeiture than in the other cases was upheld by this court. However, *Infinity Gold* involved an option to buy-back shares for breach of a share purchase agreement, not land. In upholding the forfeiture, the court emphasized evidence of the expected losses to the innocent party due to the breach by the defaulting party. The court also gave effect to the bargain because it was made by two equally sophisticated commercial parties, i.e. corporations. Those factors do not apply in this case.

[77] Michael purchased the lot from Paletta International in 2010 for $75,000. In 2017, he sold the lot to the Konialians for $1,050,000.00, plus HST. In May 2019, the lot was valued at $1.3 million. Michael had made no change or improvement to the lot. The impugned provisions of the Option Agreement would allow him to repurchase that lot for $262,500, plus HST. I observe again, on the record before me, neither Michael, nor Paletta International, have suffered any damage as a result of the Konialians failure to “commence construction” within six months of closing or substantially complete the construction 18 months after that.

[78] I recognize that a substantial windfall or a lack of damages normally does not, in itself, make a forfeiture disproportionate (*Peachtree*, at para. 27, citing *Stockloser*, at p. 100). But it can. I also recognize that gross disproportionality between the damages suffered and the amount forfeited will only rarely in and of itself render a forfeiture unconscionable (*Redstone*, at paras. 16-17, and 26). But it can. In this case, the repurchase and daily penalty provisions are so grossly disproportionate that they are

unconscionable under the first part of the *Redstone* test for unconscionability. To use the wording of Paccioco J.A. in *Scicluna*, the repurchase and daily penalty are “so manifest and so grossly disproportionate that relief from forfeiture is patently a correct result” (at para. 31)

[79] Despite this finding being sufficient to grant relief from forfeiture and set aside the Option Agreement, I add, under the second part of the *Redstone* test, that the Konialians have established that it would also be unconscionable for Michael to retain this windfall. The substantial disparity between the value of the property forfeited, the quantum of the penalty and the lack of any damage caused by the breach makes it unconscionable for Michael to retain this windfall.

(ii) Other Indicia of Unconscionability:

[80] There are also other *indicia* of unconscionability that make it unconscionable for Michael to retain the property and keep 75 per cent of the purchase price plus $270,000 in penalties in these circumstances.

[81] As a preliminary note, I would reiterate two important findings from *Peachtree* that inform my decision. First, an equitable approach to the relief from forfeiture analysis should be favoured over a strict common law approach “whenever possible” (*Peachtree*, at para. 29). Second, under such equitable approach, the enforceability of forfeiture clauses is considered “at the time of the breach rather than at the time the contract was entered” (*Peachtree*, at para. 25). The behaviour of the litigants in this case is, therefore, relevant up to and including the date of the breach.

[82] A number of other factors satisfy me that, in additional to being grossly disproportionate, the repurchase and daily penalty provisions are unconscionable.

(a) Conduct of the Parties

[83] Michael and Angelo did not conduct themselves reasonably in the face of the breach. They certainly did not act like parties who were being damaged by the delay in commencing construction. They sat by silently in the face of the breach that should have

been obvious to them as of August 22, 2017. Even when the second deadline passed (for the substantial completion of construction), neither Michael, nor Angelo said or did anything. Neither Michael nor Angelo offered any reasonable explanation for their failure to act sooner.

[84] I will say more later about whether there was a waiver in this case. But I note that Michael and Paletta International's silence over many months shows how little they were impacted by, or even cared about, the state of construction on the property.

[85] Michael deposed that he had delegated the supervision of this transaction to his brother, who was responsible for the development operations of the Bluffs. Michael deposed that he noticed that there was no building on Lot 12 when he drove by in March 2019. He was not driving by for any reason. He did not keep track of the construction because it simply "did not matter" to him. Angelo was managing the Bluffs. Michael's evidence was that he triggered the repurchase provisions because he did not want a "never-ending project." There is no evidence that he made any inquiries of Raffi, Robinson or Angelo about the reasons for the delay before he made the decision to give notice of his intention to repurchase the lot on March 8, 2019.

[86] Angelo gave evidence that he did not notice the passage of time until his brother mentioned it to him in March 2019. Angelo explained that he had many projects on the go. When Raffi reached out to him in February 2019, he did not put together that two years had passed since the closing. As far as he was concerned, it was not his responsibility to tell Raffi to speak to Michael about the development requirements. Those requirements were "there in black and white." He too made no inquiries of Raffi as to the reasons for the delay in the commencement of construction. I infer that he made no inquiries in this regard because Robinson had kept him up to date.

[87] From both Michael's and Angelo's evidence, I infer that a purchaser's compliance with the construction schedule was simply not that important to them. This is consistent with Raffi's understanding of the situation: so long as a third-party purchaser was making

efforts to obtain the requisite permits, Paletta International would not seek enforcement of the repurchase or penalty provisions. That accords with what Robinson told him.

[88] Michael and Paletta International argue that Raffi's conduct was unreasonable. They argue that the design process was delayed as a result of his indecision. They argue that the only factor for the delay was cost of the fire suppression system. As a result Raffi was not entitled to any extension or consideration under the Option Agreement.

[89] I disagree.

[90] Raffi's conduct was not unreasonable. The construction of a new home is a significant undertaking. The construction of a luxury 5,000 square foot custom home in a rural area, under management by the Niagara Conservation Authority, is a huge and complex task. Raffi put considerable effort and expense to pursue the design and construction of the home. I find that he did so diligently and reasonably. He suffered setbacks, which in my view were outside of his control. He had no incentive to delay construction. His efforts to commence construction were genuine. He was not flipping the lot or allowing a partially completed dwelling to linger (which is what Paletta International was legitimately concerned with).

[91] Through no fault of Raffi, the requirement for a fire suppression system was not identified by anyone until some five months into the design process. At that point, considerable time and effort had already been invested into the design of the bungalow. Robinson offered what appeared to be a reasonable potential solution to the difficulty: the design and installation of a $100,000 underground water tank system. Raffi spent time and money on pursuing this proposed solution. He may not have moved to do this work immediately, but other design work was ongoing.

[92] The ultimate design of the underground water tank system was significantly more involved than first anticipated. It required the excavating, blasting of bedrock and burying of giant water tanks, underground. They had to be buried deep enough that the water would not freeze. Raffi gave evidence that the tanks had to be buried in the front yard, close to the house. Nothing could be placed on top of them. The cost of this system was

almost four times the original estimate. More importantly, there were no guarantees that this system or the alternate sprinkler system would satisfy the City of Burlington's requirements. It was entirely reasonable for Raffi to conclude that, given this unanticipated requirement, he simply had to abandon the bungalow design. The degree of customization offered to purchasers in the Bluffs meant he was within his right to do so.

[93] I accept Raffi's evidence that he received and relied on assurances from Robinson that the timelines under the Option Agreement would not be strictly enforced so long as he was moving towards obtaining a building permit. I accept Raffi's evidence that Robinson told him that he was updating Angelo. I accept Raffi's evidence that these assurances figured prominently in his decision to abandon his first design. While I have found that Robinson was not an agent, his assurances to Raffi are nonetheless relevant in assessing Raffi's conduct.

[94] Raffi's understanding that the construction deadlines imposed by the Option Agreement would not be strictly enforced is consistent with Michael's and Angelo's conduct. When the first construction deadline passed on August 22, 2017, Michael and Angelo said and did nothing. Angelo's evidence also confirms that he did not strictly enforce the six-month construction deadline so long as purchasers made progress to obtain building permits and commence construction. Angelo gave evidence that he waived this deadline for three other purchasers (in 2005, 2006 and 2017) even though the Option Agreement did not provide for an extension.

[95] I also accept Raffi's evidence that Robinson told him he was keeping Angelo up to date. Robinson said so in an email to Raffi in February 2019. Keeren confirmed that Raffi was under this impression. Angelo's failure to voice any concerns about the pace of development would have re-enforced Raffi's confidence that, so long as he was taking steps to obtain building permits, there was no need for concern. Indeed, I find as a fact that neither Michael nor Angelo had any genuine concerns with the pace of construction.

[96] I note that the evidence of Robinson's statements to Raffi are not advanced in a way that amounts to hearsay. These statements are not advanced for the truth of their contents, nor used by me for that improper purpose. Rather, the statements are advanced for the fact that they were made. These statements are relevant to and provide evidence of the state of mind of the parties, informing their actions and decisions. They are, in my view, admissible for this limited use. Evidence that Robinson made certain assurances are a significant factor that informs the reasonableness of Raffi's conduct.

(b) Sophistication of the Parties:

[97] I accept the Respondents' argument that Raffi was not an unsophisticated buyer. Raffi (55 years old) earned a high school degree in Montreal. He owned and operated a jewellery store in Brampton for 30 years before retiring. The purchase of Lot 12 was his fourth recent real estate purchase.

[98] In 2019, when he swore his affidavits, he owned a home in Oakville, Ontario. He had designed and built a family home there, after tearing down an old structure. In 2011, he bought a property in Mississauga and successfully applied for severance and rezoning of the property for eight units. He did not develop or build on that property, but he did assemble a team to conduct an appeal to the Ontario Municipal Board. In 2014, he purchased a property in Mississauga. He and his spouse had intended to tear down the existing house and build a new home there, but decided in 2016 to sell that property to buy Lot 12 in the Bluffs instead. He had worked with architects, designers, general contractors and lawyers on these projects. He appreciated what was involved in the design and permitting steps.

[99] Raffi was sophisticated enough to appreciate, when he signed the APS, that 18 months to build a home was not an unreasonable timeframe. He had no concerns about it. Equally, however, he appreciated that six months to commence construction (as defined) was not a reasonable time frame. He testified that as far as he was concerned, six months was needed for the design phase alone, particularly having in mind weather restrictions on the building season.

[100] Raffi's uncontradicted evidence is that upon reviewing the APS, he became concerned that the timeline for commencing construction within six months of closing was unrealistic. He discussed his concerns with Robinson. His concerns were assuaged when Robinson told him that the provisions were meant to prevent speculation and that so long as Raffi made persistent efforts to obtain a building permit, the provisions would not be enforced. Robinson also told Raffi that he would keep Angelo informed about any delays with respect to building.

[101] Raffi was ultimately satisfied by Robinson's assurances. Had he thought that the six months to commence construction was a timeline that would be strictly enforced, he testified, he would not have signed the agreement. I accept this evidence. It was not challenged in any way.

[102] Raffi also testified that many of the clearance requirements, as he went through the process, took him by surprise. For instance, he did not know that he would need to design a fire suppression system or design a plan for managing storm water. He testified that he thought the lot was approved by the Ontario Municipal Board, so he did not think he would have to do "all that" before he could apply for a building permit. I accept his evidence in this regard as well. Again, it is left unchallenged.

[103] Angelo had been a real estate developer for over 35 years. He has been the President and CEO of Paletta International since 2002. He has been involved in dozens and dozens of substantial real estate developments. While Raffi was not an unsophisticated buyer, Raffi was no match to Angelo when it came to appreciate the complexity and significance of the development requirements imposed under the APS.

(c) Inequality in Bargaining Power and Absence of* Bona Fide *Negotiations:

[104] There was a significant imbalance in the bargaining power of these parties and a complete absence of *bona fide* negotiations. Raffi was simply presented with what amounted to a 'take it or leave it' standard form APS with a set construction schedule. The parties agree that there were no negotiations of the terms of the APS. Raffi testified that although he did not think one of the terms in the APS was reasonable, he did not

think he could change any of its terms. At that point, Robinson certainly appeared to him to be acting as an agent for the Vendor.

[105] Robinson invited Raffi to direct any questions to him. This is confirmed in an email sent by Robinson. As I have set out earlier, I accept Raffi's evidence that he questioned Robinson about the reasonableness of the requirement to commence construction within six months of closing, and that he was assured that those deadlines would not be strictly enforced. Given the amounts involved (a loss of $750,000) and Raffi's apprehensions about the six months to begin construction, it is clear to me that he believed that term would not be enforced.

[106] After the APS was signed, Raffi retained a lawyer to assist with the closing. The lawyer sent a standard letter to the vendor's lawyer, asking for a current survey, a statement of adjustments and evidence regarding title. In response, Angelo telephoned Raffi personally and threatened that if his lawyer did not "smarten up" they would lose the deal. Raffi then instructed the lawyer to withdraw the request. This set of events is confirmed by an email from Raffi's lawyer to Richard Applebaum, Paletta International's lawyer. In that email, Raffi's lawyer stated that Angelo's direct communication with Raffi, his threat to have deposit monies forfeited and to sue the Konialians for breach of contract, were highly improper.

[107] In an email exchange about an expensive watch, Angelo said to Raffi that he saw the lawyer's email and that the lawyers "need to be very careful as what she said is a complete lie. They will be held for liable [sic] and slander if they do not state true facts." To this Raffi replied, "Ya I saw that it wasn't called for. Anyway, I thing [sic] we closed and I am excited to build a wonderful house and move into it."

[108] Angelo deposed that he did not make any threats to Raffi. He asserted that he did not think the requisitions requested by Raffi's lawyer were necessary. It is not clear to me why Angelo responded to the lawyer's request as the lawyer said he did. The requests were standard ones. I am not prepared to conclude, on Angelo's say so, that the lawyer's inquiries were unusual or unreasonable. In my view, Angelo's suggestion that Raffi would

lose the deal if his lawyer made the requisite inquiries was unreasonable. Raffi, having lost out on the purchase of Lot 11, had an added emotional investment in closing the transaction. As Michael deposed, Lot 12 was a unique opportunity. Despite the otherwise friendly tone of the emails between Raffi and Angelo, Angelo's conduct could have no effect but shut down any possibility of *bona fide* negotiations about the terms of the agreement.

[109] I do not accept Angelo's evidence that he ever raised or pointed out the construction schedule in any substantive way during his discussions with Raffi before the APS was signed. He had 25 points of email contact with Raffi in those early days. But all of those communications were cursory in every way. Angelo's recollection of the specific events was otherwise not very clear. For instance, when cross-examined, he could not recall how or why the decision was made to give notice of the intention to repurchase. He could not recall his own interactions with his brother, Michael, on this point in March of 2019. He was busy with many projects and did not even notice for more than 18 months that construction on Lot 12 had not started as required. I find it difficult to accept that he accurately and reliably recalled a specific aspect of any of his conversations with Raffi in the fall of 2016, let alone this specific conversation.

(d) Unreasonable and Unfair Terms:

Six Months to "Commence Construction"

[110] Some of the terms of the Option Agreement were inherently unreasonable and unfair.

[111] The requirement to commence construction within six months of closing is unreasonable. As Raffi pointed out in his evidence, if at the time of closing he had a design in hand for a modest "cookie cutter" house, six months might be a reasonable time frame in which to obtain a building permit, excavate and pour a foundation. However, this is not a subdivision with "cookie cutter" homes. Angelo testified that the intention was for a luxury subdivision and to allow purchasers of these very expensive lots to build homes with a great deal of customization.

[112] While some purchasers in the development were able to commence construction within six months, at least three others could not. They sought waivers of this requirement, which were granted by Angelo. Although the waivers were intended for a short duration, the actual delay in starting or completing construction was significant.

[113] The Konialians were expected to design a large luxury custom home. There were no municipal services to the lot. There is an inherently complex process to get the requisite approvals from the Niagara Conservation Authority, the Region of Halton and to obtain building permits from the City of Burlington.

[114] In order to “commence construction” under para. 1 of the Option Agreement, the Purchaser was required to obtain a building permit, excavate and complete a basement and foundation for a minimum 5,000 square foot structure. To accomplish this, the purchaser would have to:

a. retain an architect or designer;

b. finalize a design of a very large home;

c. retain various consultants to do the required designs and drawings to obtain conservation approval, zoning clearance, grading certificate, mechanical and structural approvals;

d. have “working” or “permit” drawings and supporting documentation prepared and approved;

e. obtain the various clearances and approvals required for a building permit application;

f. submit and receive the building permit;

g. retain an approved builder;

h. negotiate an estimate or budget for the construction project (here the value of the construction project was $3.5 to $5.8 million); and

i. excavate the basement and fully complete the foundation for a house that is at least 5,000 square feet.

[115] I accept Raffi's evidence that the design of the house alone would take six months. His evidence in this regard accords with common sense and is confirmed by Keeren.

[116] Keeren testified that the custom design of a "normal" sized house would usually take two to four months. The preparation of working drawings, which are required for clearance and permit applications, would take another several months. Once an application for a building permit is submitted, another five to six weeks are required for approval provided there are no changes to be made. Thus, even in the case of a "normal" house, the whole six months would be used up before construction could even commence.

[117] Angelo confirmed that excavation and pouring of foundation is weather-dependent. There can be two or three months in the winter when this work cannot be done. Depending on when one obtains the building permit, additional unavoidable delays can reasonably be anticipated, indeed expected, due to weather.

[118] The six-month timeframe to "commence construction" was unreasonable, and seems calculated to produce a default. Under the Option Agreement, a purchaser like Raffi could not obtain an extension to "commence construction", even if the delay was the result of events outside of his control. The Option Agreement penalizes *bona fide* purchasers who are diligently engaged in the process of designing a home and obtaining the requisite permits, with every intention of building the home. Such a result is not rationally connected to the goals of the development.

[119] The requirement that construction be commenced six months after closing was entirely unreasonable, bordering on the impossible, in the circumstances. Intentionally or not, it is a trap for the unwary.

No Extension of the Time to "Commence Construction"

[120] While the Option Agreement allowed for an extension of the 18-month period for the substantial completion of dwelling, it made no allowance for an extension of the six months to "commence construction." This too is entirely unreasonable and unfair.

[121] Many events outside of the control of the purchaser can reasonably be expected to cause delays at this stage. For example, conservation approval can be withheld due to any number of environmental reasons unknown at the time of the purchase. Should a purchaser, despite best efforts, experience even modest delays in obtaining the requisite clearances, approvals and a building permit for reasons entirely outside of his or her control, the repurchase and daily penalty provisions are automatically triggered. A good example of the kind of delay that may arise at this stage was the requirement for a storm water management report made by the municipality in February 2018.[7]

[122] In this case, I find that the delay in commencing construction was for reasons outside Raffi's control. He was not alerted to the requirement for a fire suppression system until well into the summer of 2017, when the six-month long process of designing the bungalow was almost used up. At that time, he was assured by Robinson that a fire suppression system could be installed for $100,000. At the end of the day, when the underground tank system was designed and properly priced, it would cost four times as much.

[123] An alternative system, a sprinkler system, was considered. It was budgeted to cost $48,000. I accept Raffi's evidence that in February 2018, he abandoned the first design not just because of the costs associated with the fire suppression system but also because of the uncertainty that either solution would be approved by the City of Burlington, occasioning more delay. Both he and Keeren testified that the City of Burlington gave no assurances in this regard.

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[7] Raffi and Keeren testified that this request was made by the City of Burlington in February 2018. Robinson was able to negotiate with the City and the requirement was waived.

[124] In my view, the delays in commencing construction in this case were inherent to the custom design of a large and luxurious home and permitting process. Raffi's decision to scrap the first design and embark on the process to design a different home was reasonable in the circumstances. The delay did not arise from costs to the purchaser. Cost was a factor, as it always in in construction. But the delay arose from the requirement of a fire suppression system which caught everyone unawares. This requirement and many of the events that followed were not within the control of the purchaser. The delay in this case was due to circumstances beyond Raffi's control.

[125] Angelo admitted that he waived the requirement to commence construction within six months for some purchasers in some circumstances. He said he did so because they asked. There is no reasonable explanation for why he would not extend the same courtesy to Raffi. Raffi felt that he did not need to ask because he believed that his communications with Angelo, through Robinson, amounted to an implicit waiver of the requirement. I find that Angelo's later exercise of this discretion under the Option Agreement in Raffi's case is either entirely arbitrary or done in bad faith.

[126] Further, by failing to allow for any extensions of the six months to commence construction for reasons that are beyond the control of the purchaser, the terms of the Option Agreement are unreasonable and unfair.

Incentive for Vendor to Allow Breach to Continue

[127] The daily penalty provision of the Option Agreement is inherently unfair. It creates an incentive for the vendor to ignore or sit silently in the face of a breach of the contract for as long as possible while the daily penalty accrues. The payment of $1,000 for a breach is unconnected to any actual or anticipated damages. The payment is required on demand. The demand may be made retroactively, as it was here. Michael demanded payment of $1,000 per day retroactive to August 22, 2017. The penalty would have totalled $819,000 by November, 2019 when Michael agreed to "stop" the accrual of the penalty. The demand for payment of the $1,000 per day may be made without notice of

the breach, as it was here. In my view, the provision for the payment of $1,000 per day for delay in construction in this case is inequitable.

[128] The repurchase provision of the Option Agreement is also inherently unfair because it allows the vendor to repurchase the lot, together with any improvements, even where construction commenced within the requisite time lines, and almost completed. For instance, if a dwelling is built to 70 per cent or 80 per cent, but the purchaser encounters delays due to lack of funds, the vendor is entitled to repurchase the lot with the almost completed dwelling, still for only 25 per cent of the purchase price.

Conclusion on Unconscionability

[129] Parties to a contract are entitled to enter into an inherently unfair agreement (*Geffen v. Goodman Estate*, 1991 CanLII 69, [1991] 2 S.C.R. 353, at p. 24). That does not, however, mean that the courts will in all cases enforce such contracts. I find that the forfeiture and daily penalty provisions are grossly disproportionate to any actual or potential damages. It would be unconscionable for Michael to retain the purchase price of $1,050,000, repurchase the lot now valued at $1.3 million for $262,500 inclusive of HST and claim $270,000 in daily penalties. I also find several *indicia* of unconscionability including the unfair conduct by Michael and Paletta International; the significant steps taken by Raffi to commence construction; the disparity in the sophistication of the parties; the inequality of their bargaining positions, the absence of *bona fide* negotiations, and the inherently unreasonable terms of the Option Agreement.

[130] As a result, I decline to enforce the Option Agreement and grant the Konialians' application for relief from forfeiture.

ISSUE TWO: WAIVER AND ESTOPPEL

[131] The Konialians argue, in the alternative, that Michael waived his rights under the Option Agreement or that he is estopped from enforcing those rights as a result of the conduct of his agents, Angelo and Robinson. They argue that Angelo waived Michael's right to enforce the Option Agreement through his conduct. They also argue that Robinson was the agent for Michael (either directly or as a sub-agent through Angelo).

They add that Robinson, within the scope of his actual or ostensible authority as agent, waived Michael's rights under the Option Agreement, or made representations that estop Michael from now asserting those rights.

[132] Michael argues that Angelo's authority to deal with the Konialians was limited to approving the architectural drawings and receiving notices under the APS. He denies that Angelo waived his rights under the Option Agreement. Michael and Angelo denied that Robinson was their agent or that he had any ostensible authority. They argue that the implied representation must be that of the principal, not solely that of the agent. In this case, they argue that it was obvious that Robinson was the builder and did not speak for the developer, or Michael, and that any waiver or promises he made were his alone.

[133] There is no dispute that Angelo was Michael's agent. Michael and Angelo both offered evidence to this effect. According to Michael, Angelo was responsible for the development operations of the Bluffs. Angelo was in charge of the subdivision. The APS put positive obligations on Angelo as Michael's agent to review and approve architectural plans and receive notices to the vendor.

[134] The Konialians argue that Angelo, in turn, appointed Robinson as his (and by extension, Michael's) agent. Robinson had a contractual relationship with Paletta International. To make out Michael's waiver and estoppel, they rely on Raffi's uncontradicted evidence that Robinson told him prior to the purchase that the six months construction deadline would not be enforced.

[135] As indicated earlier, evidence of Robinson's statements to Raffi are not hearsay. These statements are not adduced for the truth of their content, but for the fact that they were made. These statements are relevant to the state of mind of the participants. They inform Raffi's understanding of the contract and the reasonableness of his subsequent conduct. His evidence that Robinson made these assurances stands uncontradicted.

[136] Michael's affidavit contains reference to out of court statements alleged to have been made by Robinson to Paletta International lawyers. These out of court statements

are inadmissible hearsay. The parties did not rely on them in argument and I have given them no effect.

[137] Both Michael and Angelo deny that Robinson was their agent. Angelo testified that Robinson was not authorized to make representations or waive enforcement of the development requirements.

Legal Principles:

[138] Agency occurs when one party (the "principal") empowers another person (the "agent") to act on behalf of, or represent, the principal. The effect of the relationship is to transfer to the agent the authority of the principal to act on his behalf, thereby enabling the agent to affect the principal's legal relationship with third parties (*Trident Holdings Ltd. v. Danand Investments Ltd.*, 1988 CanLII 194, (1988), 64 O.R. (2d) 65, (Ont. C.A.) at para. 35).

[139] Agency may be actual (express or implied) or apparent, where it results from a manifestation made by the principal to third parties (*Monachino v. Liberty Mutual Fire Insurance Company*, 2000 CanLII 5686, (2000) 47 O.R. (3d) 481, (Ont. C.A.) at paras. 33-37). Apparent or ostensible authority arises where the principal represents or permits it to be represented, by words or conduct, that another person has the authority to act on the principal's behalf. Then he is bound by the acts of that other person. There must be evidence to establish an agency relationship derived from the principal *(Hav-A-Kar*, at paras. 38-39). The onus to prove an agency relationship is on the party seeking to establish it (*Hav-A-Kar*, at para. 38).

[140] The law on waiver is summarized succinctly by Gillese J.A. in *Technicore Underground Inc. v. Toronto (City)*, 2012 ONCA 597, at para. 63:

> Waiver occurs when one party to a contract (or proceeding) takes steps that amount to foregoing reliance on some known right or defect in the performance of the other party. It will be found only where the evidence demonstrates that the party waiving had (1) a full knowledge of the deficiency that might be relied on and (2) an unequivocal and conscious intention to abandon the right to rely on it. The intention to relinquish the right must be communicated. Communication can be

> formal or informal and it may be inferred from conduct. The overriding consideration in each case is whether one party communicated a clear intention to waive a right to the other party. (see also, *Bridgesoft Systems Corp. v. British Columbia*, 2000 BCCA 313, at para. 71)

[141] Estoppel is a complex notion that requires several essential elements. It arises where a party to a contract makes a positive representation regarding a change to the entitlement under the contract, with the intention that the representation be acted upon. The statement has to be acted on to the detriment of the other party. When the party to whom the representation has been made acts on it to his or her detriment, courts have held that it would be inequitable to allow the person making the representation to then act in a contrary or inconsistent manner by insisting on the strict enforcement of the original terms of the contract (*Newton's Grove School Inc. V. J2ASM Inc.*, 2018 ONSC 7691, at para. 18-24).

[142] The oral representation or waiver of a written provision in a contract must be that of the principal, and not solely that of the alleged agent (*Hav-A-Kar*, at para. 43). An oral representation by a third party to a written contract will not defeat an obligation under that contract where (a) the alleged agent was not a party to the written agreement, (b) the contract clearly stated who the parties to the agreement were, (c) the party claiming that a representation or waiver was made was aware of who the principals of the both entities were, and (d) there are no communications between the party claiming that a representation or waiver was made and the principal, regarding the content of the alleged oral representation. Waiver or estoppel cannot arise from the unilateral actions of the alleged agent. The waiver or representation must be made within the scope of the authority given to the agent by the principal.

Application – No Waiver or Estoppel by Robinson:

[143] In this case, I am not satisfied that Robinson was the actual or ostensible agent for Michael or Paletta International. Therefore, he could not waive the requirements under the Option Agreement nor estop Michael from relying on them.

[144] I accept that Paletta International allowed Robinson to deal with prospective purchasers on their behalf. When Raffi first discovered the Bluffs in the fall of 2016, he contacted Angelo for information. Angelo put him in touch with Robinson.

[145] Robinson gave Raffi a tour of the subdivision in September 2016. He told Raffi that Robinson Homes had the exclusive right to build homes in the subdivision and that he had built most of the homes there. Advertisements for the subdivision stated that it was "developed by Paletta International," and was to be "exclusively built by" Robinson Custom Homes. Robinson Custom Homes signage was placed throughout the subdivision. I accept that Robinson acted as if he was selling the lots but there is no evidence he was, or was represented to be, authorized to legally bind Paletta International in any way. In a follow-up email after the first tour, he offered to answer any questions Raffi had. But email correspondence before me confirms that it was Angelo who emailed Raffi the APS.

[146] By the time the Konialians were ready to make an offer, Lot 11 had sold. In November 2016, Robinson gave Raffi another tour of the available lots, but none appealed to Raffi. Then Robinson told him about Lot 12 – it was not for public sale but it was owned by Michael personally. Robinson offered to approach Michael about selling it to Raffi. An email exchange between Angelo and Raffi shows that with Robinson as the go-between Raffi and Michael, the price for Lot 12 was agreed upon.

[147] In my view, Robinson acted in some respects as an agent would. At the same time, I find that Robinson was clearly identified by Angelo to Raffi from the outset as the builder. He is identified as the builder in the APS, the advertising and the signage. With his role defined as 'the builder,' he did not have ostensible authority to bind the principal (Michael or Paletta International). Raffi had 25 points of contact by email and phone with Angelo during the pre-purchase phase.

[148] While Michael and Angelo held Robinson out as their agent for some things, this does not mean he was their agent for all purposes – he could not, for example, have

entered into a binding contract to sell the property. It was clear that Robinson did not have unlimited legal authority to bind the principal(s).

[149] I also find that at the time of the sale, Robinson could not waive Michael's rights under the Option Agreement for the following reasons. First, waiver cannot occur in advance of the breach. The deficiency to be relied on must be known at the time of the waiver. Second, there is no evidence that Michael (or Angelo) ever communicated to Robinson an intention to waive reliance on the agreement. In the absence of some evidence of a communication from Michael or Angelo (as Michael's agent) to Robinson, I cannot find that Robinson's statements to Raffi or his conduct amounted to an implied representation by Michael or waiver. Waiver does not arise from the unilateral actions of an alleged agent (*Hav-A-Kar*, at para. 43).

[150] I have found that Robinson told Raffi that the six-month timeframe to commence construction would not be enforced. Raffi believed Robinson was acting as Michael's and Angelo's agent at the time. He relied on Robinson's representation and entered into a contract he would not have otherwise entered into. Raffi also made decisions during the design process, including the decision to abandon the first design, based Robinson's representation that the six-month deadline was not a "hard" deadline. He did so to his detriment. However, I am unable to conclude that Raffi did so based on anything Michael (or Angelo) represented to Robinson.

[151] Although it is possible to be estopped without consciously abandoning one's contractual rights via an agent, this is a narrowly-defined exception. It requires affirmative conduct on the part of the principal to 'hold out' the person as his or her agent. I am simply not satisfied on these facts that Robinson had the actual or ostensible authority to bind Michael, Angelo or Paletta International.

Waiver of Michael's Rights by Angelo:

[152] I am, however, satisfied that, through his subsequent conduct in the face of the breach, Angelo waived Michael's right to enforce this deadline under the Option Agreement. For Angelo to have waived the terms of the Option Agreement, there must

be evidence that Angelo knew of the deficiency (i.e. the delay in the construction), and that he, as Michael's agent, "consciously intended to abandon that right" and communicated his intention to relinquish the right, either directly or through his conduct.

[153] I reject Angelo's claim that he did not realize in February 2019, when Raffi reached out to him, of the delays in commencing construction. Angelo is an experienced and successful developer. His business was to develop and supervise construction schedules. Development schedules are the bread and butter of his business. Based on the totality of the evidence, and the evidence I do accept, I find that Angelo's assertion that he was not aware of the passage of time is not credible.

[154] I find that Angelo was kept updated by Robinson as to the Konialian's progress for commencing construction. When they had not commenced construction six months after closing, Angelo, through his conduct, chose not to enforce that deadline. His conduct in this regard is consistent with what Robinson told Raffi prior to the APS being signed: so long as Raffi was making efforts to commence construction, the six-month deadline would not be enforced. This is also consistent with how Angelo acted with respect to other purchasers on prior occasions: he waived compliance with the six-month deadline for three other purchasers, even though the Option Agreement did not provide for an extension of this term.

[155] That Angelo was kept updated as to the progress of the development is also consistent with how he responded to Raffi when Raffi reached out directly to him in early February and March, 2019. From their communications, it is clear that rather than express any concern with the delay, Angelo was prepared to approve Rob Russo as the builder, receive and review the architectural drawings and move forward with the development. It was not until Michael (at their meeting with the company lawyers) pointed out that Michael could exercise his rights under the Option Agreement to repurchase the lot, that Angelo changed his mind. But it was too late to change his mind at that point. Through his conduct, Angelo had waived Michael's rights under the Option Agreement.

[156] Michael argues that Angelo only had limited authority as his agent, and did not have the authority to waive his rights under the Option Agreement. I don't accept this argument. Michael very clearly deposed and gave evidence under cross-examination that Angelo was responsible for the development of the Bluffs. This included all aspects of the development. Angelo supervised the construction deadlines for all the other lots. There is no evidence that supervisory authority for Lot 12 lay elsewhere. There was never a question that Raffi or Robinson report to Michael on the progress of construction. Even if Angelo did not have actual authority to waive Michael's right to enforce the construction deadlines, he had the ostensible authority to do so.

[157] Waiver can be rescinded on notice to the defaulting party. Having waived compliance with the six month construction deadline from August 22, 2017 to March 8, 2019, Michael or Angelo, as Michael's agent, was required to give reasonable notice of the time required to complete the contract. They did not do so. Instead, Michael moved immediately under the Option Agreement to give notice of his intention to repurchase the lot.

[158] Michael argues that he was justified in not setting a new timeline to complete the contract because the lawyer for the Konialians mistakenly stated that they had a building permit, whereas they had only applied for one. I would not give effect to Michael's argument.

[159] The evidence before me is not disputed that the Konialians submitted the building permit application on March 4, 2019 with payment of $21,424.61. On March 8, 2019 Michael gave notice by email of his intention to repurchase the lot. This halted the Konialians efforts to pursue the building permit. The statement in the lawyer's letter that they had obtained a building permit was a minor mistake, not a deliberate misrepresentation.

[160] I accept Keeren's evidence that a building permit would have likely been issued without much undue delay. Michael waived more than 18 months of delay for the Konialians to commence construction. To rescind the waiver, he was obliged to set a

reasonable time frame for them to complete this requirement under the contract. He did not give them a reasonable time frame to do so. He gave formal notice to exercise the option to repurchase on March 21, 2019.

CONCLUSION AND REMEDY:

[161] For these Reasons, I find that the repurchase and daily penalty provision contained in paragraph 3 of the Option Agreement are unconscionable, and set it aside. The Konialians' application and relief from forfeiture are granted under s. 98 of the *Courts of Justice Act*. I also find that Angelo, in his capacity as Michael's agent, implicitly waived Michael's right to rely on this provision through his conduct.

[162] Michael Paletta's and Paletta International's application to enforce the Option Agreement is dismissed.

[163] Section 98 of the *Courts of Justice Act* permits the court to grant relief from forfeiture on such terms that are just. The Respondents' argue that terms should be imposed in this case, including a new time line for commencing and substantially completing construction, payment of damages in light of the increase in the value of the land and the daily penalty amount of $270,000 to Michael, as well as full indemnity for legal costs.

[164] Michael and Paletta International argue that these terms are necessary to send a message to the market that there will be consequences for breaching the terms of the contract in this subdivision. Otherwise, there is no recourse for Paletta International to enforce the development requirements with respect to the remaining lots on which construction has not been completed. They say that these consequences were clearly intended by the parties, and even if they are unconscionable, I should give some effect to them. Equity demands a fair and balanced result.

[165] The Konialians argue that having found paragraph 3 of the Option Agreement to be unconscionable, it must be set aside and no new terms imposed.

[166] I appreciate that there needs to be some method to meet legitimate development goals. There is clearly jurisdiction under section 98 of the *Courts of Justice Act* to impose terms that are fair and equitable. In *Rae et al v. Brooks*, 2003 BCSC 1576, terms were imposed that included a new construction schedule, the payment of a sum that represented half of the probable minimum increase in the value of the property and costs. At the same time, having found certain terms of the Option Agreement unconscionable, I must be cautious and not draft a new agreement for the parties (*Shafron v. KRG Insurance Brokers (Western) Inc.*, 2009 SCC 6, at paras. 55-578).

[167] I am not prepared to order payment of damages to Michael. I have found that Michael (and Paletta International) have suffered no damages. Had Michael demonstrated actual damages, I would have recognized them. In my view, he has not shown entitlement to any percentage of the increase in the value of the lot.

[168] I am also not prepared to set a significantly shorter timeline than the one under the Option Agreement, as requested by the Respondents. It has been sixteen months since the Konialians halted their progress towards obtaining a building permit and finalizing their contract with an approved builder. I have no evidence as to the current status of their retainer of the builder or their building application.

[169] I decline to order payment of the daily penalty to Michael from February 22, 2019, to November, 2019. I have found that in the circumstances of this case, the six months timeline to “commence construction” was woefully unreasonable. I have found that Michael and Angelo conducted themselves unfairly. I have also found that Angelo waived Michael’s rights under the Option Agreement. When Michael rescinded the waiver, he failed to set new timelines to give the Konialians a reasonable time to comply. I have found that this daily penalty, payable on demand and retroactively, is inequitable. I decline to enforce it.

[170] I agree with the Respondents that a message must be sent to the market that there are consequences for breaching terms of contract and failing to comply with development requirements. At the same time, however, a message must also be sent to

developers that the terms imposed on purchasers must be reasonable, that their conduct in the face of a breach of contract must be fair and that the consequences imposed under such contracts must be proportionate and equitable.

[171] In granting relief from forfeiture, I am inclined to impose the following terms, but invite further submissions from the parties:

a. The Konialians must “commence construction”, as it is defined in paragraph 1 of the Option Agreement, within six months from this decision. They must have their architectural plans and design approved by Michael (or his designate), acting in good faith, hire an approved builder and produce a contract with that builder when requested to do so in writing by Michael (or his designate). If they cannot “commence construction” within this time frame, they must give written notice to Michael and request an extension; provided that the delay in commencing construction is due to acts of God, strikes, or any other matter beyond the Konialians’ control and other than cost to them, a reasonable extension shall be granted;

b. The Konialians must substantially complete the construction of the dwelling, as defined in paragraph 1 of the Option Agreement, within a further 18 months from date construction is commenced. If the Konialians are unable to substantially complete construction within this timeframe, they must give written notice to Michael and request an extension; provided that the delay in commencing construction is due to acts of God, strikes, or any other matter beyond the Konialians’ control and other than cost to them, a reasonable extension shall be granted;

c. The Konialians must comply with paragraph 2 of the Option Agreement and use an approved builder. In this case, Rob Russo has been approved;

d. If the Konialians fail to comply with these terms, or if they sell, transfer or convey the Lot prior to having substantially completed the dwelling, Michael

may repurchase the Property (together with all improvements situate thereon) for $840,000, or 80 per cent of the purchase price, plus HST;

[172] The parties may advise by email whether they wish to make further submissions with respect to these proposed terms by July 3, 2020. If the parties wish to make no further submissions, then these terms will be imposed under s.98 of the *Courts of Justice Act*.

[173] There may be a question of how a vendor can attach an Option Agreement with terms and penalties such as this one to a transfer of title to land in fee simple. This question was not raised or argued before me. Therefore, I need not decide it.

[174] Rule 59.01 of the *Rules of Civil Procedure* provides that this Order is in effect from the date it is made, that date being the date such order is made by the judge whether such Order is contained in a signed endorsement, order or judgment.

COSTS OF THESE APPLICATIONS:

[175] The parties are encouraged to agree upon appropriate costs for these applications. If the parties are not able to agree on costs, I will issue a separate decision on costs based on the parties' written submissions and costs outlines that were received and sealed at the time of the hearing of these applications.

[176] If the parties agree on costs, or wish to submit any further brief submissions on costs, they are requested to notify the court by email by July 3, 2020.

("*Original signed by*")

Chozik J.

Released: June 26, 2020

CITATION: Konialian v. Paletta, 2020 ONSC 3976
COURT FILE NO.: CV-19-2373 and CV -19-1809
DATE: 20200626

ONTARIO

SUPERIOR COURT OF JUSTICE

BETWEEN:

RAFFI KONIALIAN AND TAMARA KONIALIAN,

Applicants/Respondents on Cross-Application

– and –

MICHAEL JOSEPH PALETTA and PALETTA INTERNATIONAL CORPORATION,

Respondents/Applicants on Cross-Application

REASONS FOR JUDGMENT/DECISION ON APPLICATION

Chozik J.

Released: June 26, 2020