
BULLETIN NUMBER: REDMA-07-02

TITLE: RISKS ASSOCIATED WITH PURCHASING
“PRE-SALE” RESIDENTIAL UNITS

LEGISLATION: *REAL ESTATE DEVELOPMENT MARKETING
ACT*

DATE: August 1, 2007

Pre-sale Contracts

Developers in British Columbia commonly pre-sell residential units such as strata-titled apartments and townhouses. These “pre-sales” include any residential unit that is purchased prior to the completion of construction. Typically developers enter into contracts that provide for units to be built within two years at a fixed price, and require deposits to be paid by the prospective purchasers. The deposits are held in trust by a lawyer, notary public or real estate brokerage, unless deposit protection insurance is obtained, in which case the deposits may be released to the developer.

If a proposed development does not proceed and the purchase contract is terminated, pre-sale purchasers are entitled to have their deposit money repaid. However, unless the pre-sale contract requires interest to be paid, the purchaser may not receive interest on that deposit. This is something that a purchaser will want to clarify at the time that they enter into a contract.

Obtain Professional Advice

In order to better understand the development, the prospective purchaser may wish to consult with a licensed real estate broker before entering into any contract. A real estate licensee can explain real estate terms and practices and provide information about available properties in the purchaser’s price range.

Additionally, prospective purchasers may wish to consult a lawyer to better understand their rights and obligations in respect of an existing or proposed pre-sale contract. A lawyer will be able to provide advice with respect to the purchaser’s responsibilities under the contract, including any termination or extension rights.

Review the Disclosure Statement

A prospective purchaser should carefully review the developer's Disclosure Statement. The *Real Estate Development Marketing Act* provides that a developer must not enter into a contract to sell a development unit unless a copy of the Disclosure Statement has been provided to the purchaser and the purchaser has been given a reasonable opportunity to read it.

The Disclosure Statement explains what the developer is selling and describes the purchaser's right under the *Real Estate Development Marketing Act* to cancel the pre-sale contract within seven days of signing it.

It is important for prospective purchasers, who either already have a pre-sale contract or are considering entering into one, to appreciate the risks associated with them. Some of these risks are explained below. There may also be other risks, depending on the specific terms in the pre-sale contract and the specific circumstances of the development.

Pre-sale Risks

A proposed development may be delayed, or may not proceed at all, for a variety of reasons including: inadequate sales; delays in obtaining financing or building permits; higher than expected costs for construction materials; and an inability to hire skilled construction workers.

If a proposed development is delayed beyond the completion date set out in the pre-sale contract, the contract may provide that it is terminated unless both the purchaser and developer have agreed to an extension. If market prices have increased during a delay in construction, a purchaser may be asked to pay a higher purchase price in order to extend the original contract or obtain a new contract. There is also a risk that the developer may not agree to an extension or new contract and instead sell the unit to another purchaser. A purchaser who initially sought legal advice on their pre-sale contract will be aware of any potential termination dates or may return to their lawyer for clarification of the options available. Prospective purchasers who wish to complete their purchases should, with the appropriate professional assistance, seek a written extension of their pre-sale contract before the termination date set out in that contract.

Delays in development may require prospective purchasers to arrange temporary accommodation or delay moving from their existing homes. As delays that occur in a rising market may also be accompanied by price increases, prospective purchasers should consider how to invest their purchase monies during that time so as to keep pace with any increase in real estate prices. For example, if an existing home is to be sold to fund the purchase of a proposed unit, the homeowner may wish to delay the home sale and use any increase in the home's value to help fund the ultimate purchase of the proposed unit.

There is also a risk that real estate prices may decline in the future. If the developer completes a pre-sale contract within the time set out in the contract, the purchaser

may be obligated to complete the purchase at the agreed price, even though the real estate may have declined in value.

A purchaser may wish to assign their contract to another purchaser prior to the completion date. Depending on the specific terms of the pre-sale contract, assignments may not be permissible, or may require a substantial assignment fee to be paid to the developer. The risks associated with pre-sales apply to a new purchaser who is assigned a pre-sale contract. Additionally, depending on the specific terms of an assignment, the new purchaser may not recover any payments made to the initial purchaser and developer to allow the assignment.

A pre-sale contract may allow the developer to substitute equivalent materials or make adjustments to the layout of the unit or the development.

In the current real estate market, purchasers at several developments have had their pre-sale contracts terminated and this has led to complaints about some of the risks that are described above. It is important for all prospective purchasers to appreciate those risks in order to better understand any existing pre-sale contract and make a more informed decision about whether or not to enter into a pre-sale contract.

The Superintendent of Real Estate and the Ministry of Finance are exploring the need for additional measures to help prospective buyers make informed decisions when considering pre-sale agreements. This review is expected to conclude in early Fall of 2007.

For further information on real estate transactions and contact information for government offices and industry associations, please visit our website at www.fic.gov.bc.ca/usefullinks/default.htm or the Homeowner Protection Office website at www.hpo.bc.ca/Consumer/index.htm. In addition, the Real Estate Council of British Columbia, which regulates real estate brokers, provides valuable consumer information on its website at www.recbc.ca.

Various industry groups also provide information and seminars relating to the purchase and sale of real estate. First time home buyers may wish to take advantage of these educational events to increase their knowledge in this area.

At the Financial Institutions Commission, we issue information bulletins to provide technical interpretations and positions regarding certain provisions contained in the *Real Estate Development Marketing Act* and Regulations. While the comments in a particular part of an information bulletin may relate to provisions of the law in force at the time they were made, these comments are not a substitute for the law. The reader should consider the comments in light of the relevant provisions of the law in force at the time, taking into account the effect of any relevant amendments to those provisions or relevant court decisions occurring after the date on which the comments were made. Subject to the above, an interpretation or position contained in an information bulletin generally applies as of the date on which it was published, unless otherwise specified.