

Can I Have My Deposit Back?

By Arthur J. Menor, Esq. and Elizabeth M. Jones, Esq.,
Shutts & Bowen LLP, West Palm Beach, Florida¹

Liquidated damages for a breach of contract are meant to compensate the non-breaching party for its losses, but what if the non-breaching party benefits from the breach? Can it still keep the deposit? Is a contractual provision valid that permits the seller the option of retaining the deposit as liquidated damages or suing for specific performance?

These questions were addressed by the Florida Third District Court of Appeal in the case of *San Francisco Distribution Center, LLC v. Stonemason Partners, LP*,² which found that a seller of real property may retain the deposit as liquidated damages upon a buyer's breach even though the seller may have ultimately sold the property to a third party for more than the contract price.³ In addition, the court held that the liquidated damages clause at issue was enforceable as it was not a "penalty clause" by affording a seller the option, upon buyer's breach, between enforcing the contract by specific performance or retaining the deposit as liquidated damages.⁴ This case illustrates many of the legal principles underlying a seller's remedies for a buyer's breach of a contract for purchase and sale of real estate.

Generally, upon a buyer's material breach of a real estate purchase and sale contract, the seller has two alternative remedies: 1) the seller may sue to compel specific performance of the contract, or 2) the seller may retain the property and sue for breach of contract (i.e., damages, including consequential and incidental damages).⁵ This premise is usually included within a purchase and sale contract, although the parties will typically agree that instead of damages, the seller may retain the buyer's deposit as liquidated damages in the event the buyer breaches the contract and in lieu of any other remedy including specific performance. If the parties do not stipulate to the amount of damages, the seller is able to sue for actual damages equal to the difference between the price the buyer agreed to pay for the property and the fair market value of the property as of the date of the breach.⁶ In addition, the seller could sue for any incidental and consequential damages which were "contemplated by the parties and [were the] natural and proximate result of the [buyer's] breach," unless the parties specifically exclude these types of damages in the contract.⁷ Because it is common for a buyer to deliver a deposit on the signing of a real estate contract, and because neither party wants the uncertainty of a damages remedy, it is typical to provide that the deposit may be retained by the seller as liquidated damages if the buyer defaults.

In *San Francisco Distribution*, Stonemason entered into an agreement to sell a commercial property located in Miami Beach to San Francisco Distribution for \$5.25 million.⁸ Under the remedies clause of the agreement, if San Francisco Distribution breached, Stonemason had the option of either

(1) "retain[ing] all deposit(s) paid or agreed to be paid by Buyer as agreed upon liquidated damages," or (2) pursuing specific performance of the agreement.⁹ San Francisco Distribution breached the agreement by failing to close on the property, and Stonemason sought to retain the \$400,000 deposit.¹⁰ Interestingly, in this case only \$100,000 of the deposit had been paid, but if the agreement specifically provides that deposits "agreed to be made" may be recovered, a seller is entitled to recover the unpaid portion of the deposit as well.¹¹ Stonemason subsequently sold the property for \$5.45 million to another buyer after San Francisco Distribution's breach.¹²

While San Francisco Distribution did not dispute its breach of the agreement, it argued that the liquidated damages clause was (1) unenforceable because it provided Stonemason with alternative remedies of liquidated damages or specific performance, and (2) was unconscionable in light of Stonemason subsequently selling the property for more than the contract price.¹³

In addressing the first argument, the court analyzed *Lefemine v. Baron*¹⁴ and certain pre-*Lefemine* cases.¹⁵ In *Lefemine*, the Supreme Court of Florida held that a liquidated damages clause was unenforceable where the contract gave the seller the option of exercising the liquidated damages provision or suing the defaulting buyer to recover actual damages.¹⁶ In reaching this conclusion, the Court established a two-part test to determine if a liquidated damages provision is enforceable.¹⁷ First, "damages consequent upon a breach must not be readily ascertainable."¹⁸ Second, the agreed-upon amount to be forfeited must not be "grossly disproportionate to any damages that might reasonably be expected to follow from a breach as to show that the parties could have intended only to induce full performance, rather than to liquidate their damages."¹⁹

Prior to *Lefemine*, the Court held in *Hyman v. Cohen*²⁰ that where the parties actually intend to liquidate their damages, the provision is valid, but if the parties' real intentions are to induce performance under the contract, then the provision is unenforceable.²¹ In *Pappas v. Deringer*,²² the Third District Court of Appeal held that a liquidated damages clause in a lease agreement was an unenforceable "penalty clause" because it gave the landlord the option of retaining the security deposit as liquidated damages upon default by the tenant or suing for a greater amount of damages.²³ This was applied to a real estate contract in *Cortes v. Adair*,²⁴ where the Third District Court of Appeal found a liquidated damages clause to be unenforceable because the provision gave the seller the option of retaining the deposit or suing in law or equity to enforce its rights under the agreement.²⁵ The Court in *Lefemine* agreed with the underlying principles of both

Pappas and *Cortes*, in that a contract which gives the seller the option between liquidated damages and suing for actual damages “indicates an intent to penalize the defaulting buyer and negates the intent to liquidate damages in the event of a breach.”²⁶ Most importantly, the Court expressly noted that it was not “imply[ing] that a liquidated damages clause which merely provided the option of pursuing equitable remedies would be unenforceable.”²⁷

San Francisco Distribution argued that specific performance is “the simple equivalent of a claim for damages” and, therefore, is unenforceable under *Lefemine*.²⁸ The court disagreed, finding that “a suit for specific performance seeks equitable relief that requires the breaching party to perform its obligations under the agreement.”²⁹

Consequently, the provision in the San Francisco Distribution agreement was in accordance with *Lefemine* and its implications because it provided for an equitable remedy alternative to liquidated damages.³⁰ Although the distinction is subtle, the court’s result does appear to give a seller the option of pursuing specific performance if the contract price is higher than the market price or, as Stonemason did, retaining the deposit and selling at a higher market price. Typically, to provide certainty as to the amount of damages in the event of a buyer default, a buyer will try to negotiate away a seller’s remedy of specific performance in the purchase and sale agreement in an attempt to limit a seller’s remedy solely to the amount of the deposit.

Furthermore, San Francisco Distribution contended that damages were readily ascertainable at the time of breach.³¹ In response, the court emphasized that the relevant inquiry is whether damages were ascertainable at the time of entering into the contract.³² When addressing the relevant inquiry, Florida courts have held that the fluctuating nature of the real estate market makes it “generally impossible to say at the time a contract for sale is drawn what the vendor’s loss (if any) will be should the contract be breached.”³³

As to the second part of the *Lefemine* test, the court analyzed whether San Francisco Distribution’s forfeiture of the deposit, equaling 7.6% of the contract price, was grossly disproportionate to any damages that might be reasonably expected to flow from a breach.³⁴ The court found that it was not, observing that Florida courts routinely hold that a forfeiture amount of 10% or less is reasonable.³⁵

Finally, as San Francisco Distribution’s last argument, it contended that the amount of liquidated damages was unconscionable because Stonemason suffered no damages in light of it ultimately selling the property to a subsequent buyer for more than the original contract price.³⁶ Under the common law doctrine of unconscionability, courts may “prevent the enforcement of contractual provisions [wherein] one party seeks to gain an unjust and undeserved advantage which it would be inequitable to permit him to enforce.”³⁷ The court disagreed with San Francisco Distribution, finding that the

argument was not novel and had failed before.³⁸ In both *Hot Developers, Inc. v. Willow Lake Estates, Inc.* and *Bradley v. Sanchez*, a liquidated damages clause was enforced despite the fact that the sellers in both instances sold the property for more than the original contract price.³⁹ Essentially, the argument failed because it solely took into account the ultimate sales price while “ignoring the contractual provision itself and other aspects of potential damages consequent to a buyer’s breach,” such as brokers’ commissions, title search fees, and survey costs.⁴⁰ In addition, the argument overlooked Stonemason’s carrying costs during this time and that fifty percent of the forfeited deposit was to be distributed to the brokers involved in the transaction.⁴¹

The *San Francisco Distribution* case answers a question left partially open in *Lefemine*—a contract can validly provide a seller with the option of retaining the deposit as liquidated damages or sue for specific performance. It also provides a good summary of Florida law on a seller’s remedies for default under a contract for purchase and sale of real estate. So, to answer the question posed in the first sentence of this article—no, you may not have your deposit back. 📌

Elizabeth M. Jones is an associate in the West Palm Beach office of Shutts & Bowen LLP and a member of the Real Estate Practice Group. Ms. Jones is a member of the Landlord/Tenant and Commercial Real Estate Committees of the RPPTL Section of The Florida Bar. She is also a published author and has presented on diverse topics in the legal field.



E. JONES



A. MENOR

Arthur J. Menor is a partner in the West Palm Beach office of Shutts & Bowen LLP. He earned his undergraduate and J.D. degrees from the University of Florida. Mr. Menor is a Florida Bar Board Certified Real Estate Lawyer and a fellow in the American College of Real Estate Lawyers. He is the past Chair of the Landlord/Tenant Committee and the Commercial Real Estate Committee and is the current Chair of the Problems Study Committee of the RPPTL Section of The Florida Bar and is a frequent author and lecturer on commercial real estate law issues.

Endnotes

- 1 The authors would like to acknowledge the substantial assistance in the preparation of this article provided by Daniel Naydenov, a law student at the School of Law at Vanderbilt University.
- 2 No. 3D13–2320, 2014 WL 1491633, at *1 (Fla. 3d DCA Apr. 16, 2014), 39 Fla. L. Weekly D790a.
- 3 *Id.*
- 4 *Id.* at *2.
- 5 *Frank Silvestri, Inc. v. Hilltop Developers, Inc.*, 418 So. 2d 1201, 1203 (Fla. 5th DCA 1982).
- 6 *Clements v. Leonard*, 70 So. 2d 840, 843 (Fla. 1954).
- 7 *Buschman v. Clark*, 583 So. 2d 799, 800 (Fla. 1st DCA 1991).
- 8 *San Francisco Distribution*, 2014 WL 1491633, at *1.

- 9 *Id.*
10 *Id.*
11 See *Bradley v. Sanchez*, 943 So. 2d 218, 222 (Fla. 3d DCA 2006).
12 *San Francisco Distribution*, 2014 WL 1491633, at *3.
13 *Id.* at *2.
14 573 So. 2d 326, 328 (Fla. 1991).
15 See generally *San Francisco Distribution*, 2014 WL 1491633, at *2.
16 *Lefemine*, 573 So. 2d at 330.
17 *Id.* at 328.
18 *Id.*
19 *Id.*
20 73 So. 2d 393, 398 (Fla. 1954).
21 *Hyman*, 73 So. 2d at 398.
22 145 So. 2d 770 (Fla. 3d DCA 1962).
23 *Pappas v. Deringer*, 145 So. 2d 770, 773 (Fla. 3d DCA 1962).
24 494 So. 2d 523, 524 (Fla. 3d DCA 1986).
25 See *id.*
26 *Lefemine*, 573 So. 2d at 329.
27 *Id.* at 330 n.5.
28 *San Francisco Distribution*, 2014 WL 1491633, at *1.
29 *Id.* at *3 (citing *Mineo v. Lakeside Village of Davie, LLC*, 983 So. 2d 20, 22 (Fla. 4th DCA 2008)).
30 See *id.* at *3.
31 See *id.* at *3 n.6.
32 See *id.* at *2 n.5.
33 *Hutchison v. Tompkins*, 259 So. 2d 129, 132 (Fla. 1972); see also *Hot Developers, Inc. v. Willow Lake Estates, Inc.*, 950 So. 2d 537, 540 (Fla. 4th DCA 2007).
34 *San Francisco Distribution*, 2014 WL 1491633, at *3.
35 See *Kirkland v. Ocean Key Associates, Ltd.*, No. 07-10030-CIV, 2007 WL 3343083, at *3 (S.D. Fla. Nov. 8, 2007) (10% held reasonable); *Hot Developers, Inc. v. Willow Lake Estates, Inc.*, 950 So. 2d 537, 541-42 (Fla. 4th DCA 2007) (9.65% upheld, discussed ranges from 4.85% to 22% held to be reasonable); *Bloom v. Chandler*, 530 So. 2d 341, 342 (Fla. 4th DCA 1988) (upholding liquidated damages clause equal to 22% of the purchase price); *Hooper v. Breneman*, 417 So. 2d 315, 318 (Fla. 5th DCA 1982) (upholding liquidated damages provision calling for forfeiture of 13.3% of the purchase price); *Ivanov v. Sobel*, 654 So. 2d 991, 992 (Fla. 3d DCA 1995) (10% held not to be grossly disproportionate); *McGuinness v. Prospect Aragon, LLC*, 981 So. 2d 496, 499 (Fla. 3d DCA 2008) (holding 8% of the purchase price as neither a penalty or unconscionable).
36 *San Francisco Distribution*, 2014 WL 1491633, at *3.
37 *Basulto v. Hialeah Automotive*, 141 So. 3d 1145, 1157 (Fla. 2014) (internal quotation marks omitted).
38 *San Francisco Distribution*, 2014 WL 1491633, at *4.
39 *Id.* (citing *Hot Developers, Inc.* 950 So. 2d at 537; *Bradley*, 943 So. 2d at 218).
40 *Id.* at *3.
41 *Id.* at *3 n.7.

THE
**Florida
BAR**
PODCAST

Listen to on-demand educational interviews and stay on top of what's happening with The Florida Bar.

LISTEN FOR FREE:
www.floridabar.org/PRI



Download The Legal Talk Network Apps:



 LEGAL TALK NETWORK
www.legaltalknetwork.com