

**REAL ESTATE 101:**  
**WHEN YOUR NONREFUNDABLE DEPOSIT MIGHT BE REFUNDABLE**

**By Paul Rovella**

**The Pinnacle**

**July 2010**

If you have ever purchased or sold real estate, you may have been in a situation where a nonrefundable deposit on the purchase price was negotiated. Generally, a nonrefundable deposit is requested where one or more selling parties feel that there is some level of uncertainty that the deal will be completed. The deposit is nonrefundable because if the sale is lost for any reason, the buyer does not get the deposit back. If a nonrefundable deposit is agreed upon, then there is motivation for the buyer to complete the transaction, and if terminated, the seller will at least receive some amount of compensation for costs incurred in the transaction, and lost time and/or sale.

An example of a situation where nonrefundable deposits are typically negotiated is where a buyer and seller agree to the purchase and sale of a portion of an undeveloped lot subject to a pending subdivision application. In such a transaction, the parties may agree to a nonrefundable deposit which could compensate the seller for the lost sale if the application is not approved.

Until recently, a nonrefundable deposit was just that – a nonrefundable deposit. However, in the 2010 case of *Kuish v. Smith*, the California Court of Appeals decided that a nonrefundable deposit of \$620,000 in the purchase and sale of a \$14 million home was determined to be refundable, and the Court ordered the return of the deposit to the buyer.

The facts of the case were that Mr. Kuish agreed to purchase the home in Laguna Beach from Mr. and Mrs. Smith for \$14 million. Under the negotiated agreement, Kuish was required to make payments to the Smiths totaling \$620,000 which were deemed “non-refundable” deposits. Within a year from the date of the agreement, Kuish cancelled the contract. The Smiths then sold the same property to third party buyer for \$15 million, which was \$1 million more than the sales price they had agreed to with Kuish. Kuish demanded the return of the “non-refundable” deposits, and the Smiths refused. Kuish sued the Smiths in Orange County Superior Court to recover the \$620,000.

The trial court found in favor of the Smiths, concluding that the nonrefundable deposit was negotiated consideration for the transaction. The Court of Appeals reversed the trial court decision, stating that the Smiths incurred no damages where, after the Kuish cancelled the contract, they resold the property for a higher price. The Court of Appeals relied on California Civil Code section 3307, which states: “The detriment caused by the breach of an agreement to purchase an estate in real property is deemed to be the excess, if any, of the amount which would have been due to the seller under the contract over the value of the property to him or her, consequential damages according to proof, and interest.” The Court of Appeals determined that since the Smiths were able to sell their property for more than they would have received from

Kuish, there were no damages, and Kuish should be entitled to a refund of his “non-refundable” deposits.

In light of the Court of Appeals decision in *Kuish v. Smith*, real property sellers or real estate agents on their behalf, may wish to negotiate for “liquidated damages” rather than a nonrefundable deposit. “Liquidated damages” are a specific sum of money agreed to by the parties in a contract as a reasonable estimate of the damages to be incurred if the contract is breached by one of the parties. Liquidated damages provisions are usually used in situations where it may be difficult to determine the exact amount of damages that would be incurred as a result of a breach of contract. Although the Court of Appeals’ decision stated that its reasoning might apply to liquidated damages provisions, it acknowledged that such provisions are presumed to be valid, and thus more difficult to overturn.

This column is the work product of Lombardo & Gilles, LLP, which has offices in Hollister, Chowchilla, and Salinas. Paul Rovella is an attorney with Lombardo & Gilles, LLP. You may contact the author at (831) 630-1722 or [paul@lomgil.com](mailto:paul@lomgil.com). Mail your questions to Paul Rovella, It’s the Law, c/o The Pinnacle, 380 San Benito St., Hollister, CA 95023.