Bidding Wars: the Successful Loser!

By Brian Madigan LL.B.

You might think that having won the bidding war, Paul would be quite happy. And, he was for a bit. But, here's what happened.

The housing market was quite active, and like a number of cautious house hunters, Paul was encouraged to put in an Offer on some houses. His realtor was conservative, and Paul always seemed to lose out in the bidding process.

So, one day, Paul went to visit an Open House. He was shown through the premises by the listing agent. Given the track record with the previous agent, he thought that this time he would go with the listing realtor as his agent. The house was listed at $449,000. Initially, he wondered whether he might submit a rather high Offer at $445,000.

The listing agent said, there's going to be a bidding war, rather than lose out again, you should put in your very best Offer, first time around. So, Paul did. He had lost out on 3 other properties, and he did not want to lose this one. He was also told that one other prospective purchaser had lost out 4 times and was determined to get this house.

Paul decided to submit an Offer at $495,000. This was a bidding war with 6 other competing offers. A clause conditional on financing, lawyer's approval or home inspection would all be foolish, the result being that Paul omitted these cautionary items.

The good news was that he was the successful bidder. **At $495,000 he had won the war!** No one else had submitted an Offer nearly that high.

All was well for a few days, until Paul received a call from his mortgage broker. The appraisal came in at $445,000. He could get first mortgage financing for 95% of that amount, or $422,750. Paul was $72,250 short on this deal. Paul had put down $30,000 as a deposit on this deal and he thought that was all the money he really needed.

The agent told Paul not to worry, she would call the appraiser and tell him that the value of this property had gone up. There was a bidding war and this resulted in the property selling at a price substantially higher than other houses had been sold earlier in the year.

Unfortunately, the appraiser was not impressed. It was her job to come up with an independent assessment of the value of the property. What was the market value? What would other purchasers pay? She was not prepared to consider the relevance of Paul's own Offer. It might have been ill-informed and made in a panic. So, the **appraised** value stood, **$445,000**.

However, the real problem arose on the day of closing. Paul did not have sufficient funds to close the deal. Accordingly, he defaulted on the closing. The vendors kept Paul's $30,000 deposit. You might think that was a bad day for Paul, but it gets worse.

The vendors put the property back on the market. The agent calls the next higher bidder who actually had come in at $455,000, but he has already bought something else.

It's a little later in the year, and other purchasers wonder if something is the matter with the property; nevertheless it sells rather quickly to close within 90 days. Only one slight problem, it sells for $445,000.

So, what does this mean to Paul?

Well, the vendors are to be placed in the same position as they would be in, as far as money is concerned, as if Paul had completed the agreement on time as agreed. They tally up their expenses and find the following:

Costs of storage ($750/month)
Costs of moving ($3,500)
Cost of 3 months utilities ($800/month)
Cost of 3 months insurance ($250/month)
Cost of 3 months taxes ($550/month)
Cost of 3 more months on the mortgage (interest component only, $300,000 first)
Increased rate of interest on their mortgage (it went from 5% to 6.5%)
Legal fees and disbursements for the second transaction (otherwise unnecessary)
Loss of use of the net proceeds of sale ($195,000 being $495,000 less first mortgage)

So, what would all this add up to? (**usual losses**)

$5,750 for storage and moving
$4,800 for utilities, taxes, and insurance
$3,750 in regular mortgage interest
$1,125 in bonus interest
$1,500 in legal fees
$3,778 (computed at 7.75%)

$20,703

The vendors were under a duty to mitigate their losses. So, they did as best they could. Paul was to buy the property with a June 30th closing. The house had a swimming pool and air conditioning. It was an additional $2,750 to open the pool and have it running all summer and a further $1,500 keep the air conditioning turned up. Don't forget $1,750 for landscaping and maintenance.

So, another group of expenses for **seasonal losses**:

$2,750 for the pool
$1,500 for air conditioning
$1,750 for landscaping

$6,000.00

And, one more item. Don't forget, the lawyer's not working for free in this lawsuit, so you can add another $15,000.

So, how do you figure out how much Paul owes?

$495,000 the original sale price
$445,000 the eventual sale price

That means $50,000 is the differential.

You need to add up the following:

$50,000 for the **differential**
$26,703 for additional **expenses** (usual and seasonal)
$15,000 for legal **costs**

That means the total amount owed by Paul is $91,703. The only good news for Paul now, is that he has already paid $30,000 because that was the deposit. However, he now has to come up with another $61,703 for a house that he doesn't own.

That's an expensive lesson, and we didn't take into account any of his own losses, expenses or legal fees.

So, who won the bidding war?

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