Interest at Closing Time

This article is not referring to Leonard Cohen or last call at your favourite watering hole. It is about real estate transactions where for one reason or another, the purchase price is not able to be paid on the closing date (possession date). In the typical real estate purchase, the full purchase price must be provided to the Seller by 12 noon on the closing date. No money, no possession.

In some situations the Buyers' money may be delayed, from their bank, or from the sale of their own home. A Seller may still be willing to allow the Buyer to take possession of the home. There are 2 issues that you need to understand:

1) Why should interest be charged to a Buyer?

When a Buyer is unable to provide the full purchase price on possession date, the Seller can choose to allow possession on a tenancy-at-will basis. The tenancy-at-will provides that the Buyer pays interest at a predetermined rate, and if the deal falls through the Buyer agrees to vacate in 48 hours. A Buyer could negotiate with the Seller that no interest be paid; but in my experience this is done in the rarest of circumstances.

The Buyer is charged interest to compensate the Seller's lost opportunity to invest the money. In some cases, the Seller may also have a continuing obligation to pay a mortgage that will be paid off from the sale proceeds. The payment of interest can also be an incentive to the Buyer to complete their financing as soon as possible; there is no free ride while the Seller patiently waits for their money.

During the time the Buyer is paying interest to the Seller, he or she is not paying interest on their mortgage, as it has not been approved at this time. In other words, the Buyer is not paying 2 forms of interest at the same time.

2) What rate of interest should be charged to the Buyer?

The answer depends on who is at fault for the money not being provided to the Seller at closing. If it is the Buyer, the customary rate charged in Medicine Hat is Alberta Treasury Branches Prime + 3%. On a $300,000 mortgage, the interest payment is approximately $49.32 per day.

If the Seller is at fault, the interest rate typically will be based on the Buyers own mortgage amount, at the Buyers own interest rate. This rate of interest would be paid until the Seller could provide the Buyer with the required documents to complete the sale

In many cases the amount of interest paid by the Buyer is not significant, and understanding the mechanics of why interest is charged can reduce the stress of not closing on time.

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Date: 2011.06.20 22:11:02 -06'00'