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November 23, 2013

Tarion: Buyers may not be able to sue for claims exceeding warranty limits

Buyers should check their purchase agreements to see whether the liability limitation clause is included

A recent court decision raises the thorny issue of whether it should be legal for builders to restrict the ability of new home and condo purchasers from suing them for deficiency claims exceeding the limits of the Tarion new home warranty.

The case arose at West Harbour City, a 510-unit residential condominium project on downtown Fleet St. It was developed by West Harbour City (I) Residences Corp., a subsidiary of Plazacorp Investments.

The developer has more than 5,000 condominium units already built or under construction in Toronto. Its projects can be found in Yorkville, North Toronto, King West, Queen West, Lawrence Park, Liberty Village, the St. Lawrence Neighbourhood, Harbourfront, and Mt. Pleasant Village.

When the first phase of the West Harbour City project was completed, it was registered as Toronto Standard Condominium Corporation No. 2095.

During the project's marketing period, the small print in the agreements of purchase and sale stated that the builder's liability for deficiency claims in the units could not exceed the limits of the Tarion warranty set out in the Ontario New Home Warranties Plan Act.

As a result, owners in the project would be prevented from suing the builder for deficiency claims beyond the amounts of the Tarion warranty.

After the condominium corporation was created, and while the developer's nominees controlled the board of directors, the builder board entered into an agreement with the developer which restricted the right of purchasers to sue the developer. The board also passed a bylaw which mirrored the terms of the agreement, and the bylaw was registered on title to provide notice to subsequent purchasers.

After the units had been sold and control of the condo board turned over to the unit owners, the condominium board asked the Ontario Superior Court to set aside the bylaw and the agreement so that unit owners would be able to sue the developer for deficiency claims exceeding the Tarion warranty.

The condo board's position was that the bylaw and agreement were beyond the powers of the condominium corporation, and that no reasonable board of directors would have agreed to it.

The developer argued that it was entitled to limit its liability to the Tarion provisions, and it did so in the only way it could, by way of agreements with the purchasers and the condominium corporation.

In his decision, Superior Court Justice David L. Corbett ruled that a developer is indeed entitled to limit its risk, and it effectively did so by an agreement to this effect with the condominium corporation which it controlled at the time. The agreement was properly disclosed in advance to prospective purchasers, and registered on title so that subsequent owners would have notice of it.

"There is nothing illegitimate," the judge wrote, "about a developer seeking to limit its risk in this way, provided, of course, it does not seek to contract out of the statutory requirements (of the Tarion legislation)."

Denise Lash is a partner in the condominium law group at the Heenan Blaikie law firm in Toronto. She told me that she thinks this is a "terrible decision."

"I agree," she wrote me in an email, "that as long as disclosure is made upfront to purchasers and that purchasers understand the nature of such disclosure, then they are making an informed purchase.

"The problem is that in this case, the average purchaser would not understand what 'limiting liability to Tarion warranty' in the form of an agreement would somehow have a significant financial impact on them in the first few years of ownership. Upfront, clear and understandable disclosure - I am all for it. But this was not the case here."

I understand the decision may be appealed, but in the meantime, the Ontario government might want to consider whether this type of limitation is in the public interest, or whether it should be outlawed.

Buyers in Plazacorp projects should check their purchase agreements to see whether the liability limitation clause is included.

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Toronto Standard Condominium Corporation No. 2095 v. West Harbour City (I) Residences Corp., 2013 ONSC 5987 (CanLII)

Date:	2013-09-23
Docket:	CV-12-453714; 2095
URL:	http://canlii.ca/t/g0nkr
Citation:	Toronto Standard Condominium Corporation No. 2095 v. West Harbour City (I) Residences Corp., 2013 ONSC 5987 (CanLII), <http://canlii.ca/t/g0nkr> retrieved on 2013-12-01
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CITATION: Toronto Standard Condominium Corporation No. 2095 v. West Harbour City (I) Residences Corp., 2013 ONSC 5987
COURT FILE NO.: CV-12-453714
DATE: 20130923

SUPERIOR COURT OF JUSTICE - ONTARIO

B E T W E E N:	)	
TORONTO STANDARD CONDOMINIUM CORPORATION NO. 2095 Applicant	)	*Jonathan H. Fine* for the Applicant
- and -	)	
WEST HARBOUR CITY (I) RESIDENCES CORP. Respondent	)	*Richard P. Hoffman* for the Respondent
	)	**HEARD:** October 15, 2012

ENDORSEMENT

D.L. CORBETT J.

[1] The applicant seeks a declaration that one of its by-laws and an agreement between it and the respondent are "void and of no force or effect".

[2] The impugned agreement and by-law were part of the arrangements under which the respondent developed and built a condominium project. The agreement limits the respondent's liability for deficiency claims arising from the project, but in a manner consistent with the provisions of the *Ontario New Home Warranties Plan Act*, R.S.O. 1990, c.O.31 ("*ONHWP Act*"). The by-law requires the applicant to enter into the agreement, and purports to prevent the applicant from terminating or breaching the agreement.

[3] I have my doubts about certain aspects of the by-law. I doubt, for example, that the original board can prohibit amendment or repeal of a by-law. However, I do not doubt that the initial board may enter into an agreement respecting construction warranties and deficiencies, and that this agreement may bind the applicant into the future. That is the situation here, and accordingly the application must be dismissed.

The Impugned Agreement and By-Law

[4] The respondent developed and built a residential condominium project. The applicant was formed to own the common elements of the project and to manage the condominium on behalf of its unitholders.

[5] This was a typical residential condominium project. The respondent sold units in the project pursuant to agreements of purchase and sale. Those agreements of purchase and sale limited the recourse that purchasers had against the respondent and put the purchasers on notice that the liability of the respondent to the condominium corporation would be limited in similar fashion.

[6] When the condominium corporation was organized, its original directors were nominees of the respondent (which, at that time, owned all of the units in the condominium). This original board entered into the impugned agreement with the respondent under which the respondent's liability to the applicant was limited. The original board also enacted By-law #2, which mirrored the terms of the agreement. The by-law and agreement were registered on title to the condominium project, to give notice to all prospective purchasers of condominium units that the liability of the developer to the condominium corporation was limited.

[7] The applicant says that the by-law and the agreement were *ultra vires* the board of the applicant and are contrary to the *Condominium Act*, 1998, S.O. 1998, c. 19. They say that the agreement was not in the best interests of the applicant, and that no reasonable board of directors would have agreed to it.

[8] The respondent says that, as a developer and builder, it is entitled to limit its liability to the statutory provisions of applicable legislation. It has done so in agreements of purchase and sale with individual unit-owners. In the impugned agreement it has done so with the condominium corporation. There is no other practical way for the developer to limit its liability.

Issue #1 – Are the By-Law and Agreement *Ultra Vires*?

[9] The applicant argues that the impugned by-law is not within the enumerated subjects provided in s.56 of the *Condominium Act*.

[10] Subsection 56(1) provides, among other things:

> The board may, by resolution, make, amend or repeal by-laws, not contrary to this Act or to the declaration,
>
> (l) to govern the management of the property;
>
> (m) to govern the use and management of the assets of the corporation;
>
> (p) to govern the conduct generally of the affairs of the corporation.

[11] The applicant argues that these paragraphs of s.56(1) are too general to encompass the impugned by-law and agreement, I do not agree. It is a core part of the applicant's business to manage its relationship with the persons who developed and built the condominium. As indicated during oral argument, it would be within the Board's jurisdiction to assert, prosecute and settle a claim against the respondent. It follows, then, that it is within the Board's jurisdiction to decide not to do any of these things and to embody that decision in an agreement.

[12] None of the cases relied upon by the applicant assist it on this issue. In each, the court was concerned with the board's ability to pass rules or by-laws that restrict unitholders from doing what they like with their units. Balancing the collective interests of all unitholders and the freedom of individual unitholders, has nothing to do with the issues in the case at bar.[1]

Issue #2 – Are the Impugned By-law and Agreement Unreasonable?

[13] The affairs of the condominium corporation are managed by its Board of Directors (*Condominium Act*, s.27(1)). This Board was initially appointed by the declarant (in this case, the respondent), who owned all of the units in the condominium at the time the first board was appointed (*Condominium Act*,s.42(1)). After the condominium was transferred, a new board was elected by the unit owners (*Condominium Act*, s.28(1)).

[14] The Board of a condominium, whether elected by the declarant, or subsequently by the new unit owners, is required to act "honestly and in good faith" and to "exercise the care and skill that a reasonably prudent person would exercise in comparable circumstances" (*Condominium Act*, s.37(1)).

[15] The applicant argues that "no reasonably prudent person" would enter into this agreement or enact this by-law. The applicant received no consideration for limiting its recourse against the respondent, something no reasonable arm's length person would do.

[16] The answer to this objection is clear: there was consideration for the agreement limiting recourse against the respondent. The consideration was the respondent's agreement to transfer the project to the condominium corporation and the unit owners. It developed and sold the project on the basis that its liability would be limited, as set out in the agreement (and in the agreements of purchase and sale with the unit owners). It was entitled to do this. If purchasers did not wish to buy units on this basis, they did not have to do so.

[17] In this regard, I note that the limitations on the respondent's liability to the applicant were included in the original disclosure made to unit-purchasers, are contained in the agreements of purchase and sale with those unit holders, and were registered on title to the project once the by-law was enacted. In this way, owners and potential owners had notice of the limitation of the respondent's liability in respect to the project.

[18] During oral argument I asked Mr. Fine a series of questions around this point. If the respondent had been selling freehold homes, it would have been able to limit its liability to purchasers as a matter of contract law. The respondent is entitled to limit its liability to individual condominium owners in regards to claims respecting their individual units. Conceptually, there is no reason why the respondent should not be entitled to limit its liability in respect to claims respecting the common elements of the project. Nothing in the *Condominium Act*, the *ONHWP Act*, or any other provincial legislation, precludes a developer from limiting its liability in respect to common elements. Indeed, the provisions of the *ONHWP Act* respecting common elements in new condominiums suggest the precise opposite: a developer may not contract out of the provisions of that *Act*, implying that in other respects the developer may contract out of the common law.

[19] The law recognizes that a pre-turnover board of directors, as proxy for the developer, does not owe fiduciary duties to individual unitholders. They do no more than organize the affairs of the corporation in the manner set out in the declaration, and as disclosed to unitholders at the time that they purchase their condominiums.[2]

[20] If it is lawful for a developer to limit its liability in respect to common elements of a condominium, how is this done if not in the manner done in this case? The applicant has no answer, except to note (correctly), that it would be open to the developer to seek such an agreement from the condominium corporation after it had turned the project over to the new purchasers. But that would not work. The limitation of liability is a condition the developer has for developing and selling the project: once the unitholders have purchased their units, they would indeed be foolish to surrender any rights against the declarant for no consideration. By analogy, this would be the same as prohibiting a builder of freehold homes from limiting its liability in its agreements of purchase and sale because it could seek to do so after entering into its agreements of purchase and sale.

Issue #3 – Are the By-Law and Agreement Inconsistent with the *Condominium Act*?

[21] The applicant argues that the impugned by-law and agreement are inconsistent with the *Condominium Act* in the following ways:

(a) they limit the rights of the applicant to manage the property and affairs of the condominium corporation (by limiting remedies available for construction deficiencies);

(b) they limit the condominium corporation's access to the courts for matters not within the ambit of Tarion's jurisdiction;

(c) they cause Tarion to be the sole and final arbiter of construction deficiency issues; and

(d) they purport to cause the applicant to indemnify the respondent if it sues the respondent in contravention of the impugned agreement;

(e) By purporting it prohibit the applicant from terminating the agreement following the turnover meeting.

[22] If the impugned by-law and agreement were the product of settlement negotiations between the applicant and the respondent, and involved payment of some sort of consideration for the settlement, there would be no suggestion that the impugned documents were contrary to the *Condominium Act*. It is the wisdom of the business deal, and not the authority of the applicant's Board to make it, that is the issue here.

[23] As I have indicated already, I am not sanguine that one board of directors may prohibit future boards from amending or repealing the corporation's by-laws. I am also not persuaded that the respondent, as a party to the agreement, has standing to challenge corporate action taken by the applicant in respect to its by-laws. However, these arguments were not raised before me by the parties. And none of this would diminish the respondent's rights under the agreement itself. The applicant may not unilaterally terminate or breach the agreement with impunity, a proposition that remains valid even if the impugned by-law is amended or repealed.

Other Issues

[24] The respondent raised two procedural issues during argument: first, whether this application must be mediated/arbitrated, and second, whether the application is premature.

[25] Subsection 132(1) of the *Condominium Act* provides that disputes arising from an agreement between the condominium corporation and the declarant shall be mediated/arbitrated. This provision does not encompass applications concerning the validity of an agreement, but rather disputes under valid agreements. In any event, this provision does not cover applications to determine the validity of corporate by-laws.

[26] The respondent argued, on the strength of *McKinstry* v. *York Condominium Corp. No. 472* 2003 CanLII 22436 (ON SC), (2003) 15 R.P.R. (4th) 181, 68 O.R. (3d) 557 (S.C.J.), per Juriansz J. (as he then was), that an expansive reading of s.132(4) should lead the court to decide that the matter should go to mediation. I do not agree. Justice Juriansz concluded that a "disagreement" and the economic consequences of that "disagreement" ought to both go to mediation, in order to secure the legislature's clear intention that disputes within a condominium ought to go to mediation rather than to court. I see this logic as having no application to a situation of conflict between the condominium and the declarant after control of the condominium has passed to the individual unit holders.

[27] The respondent argues that the application is premature, since it is not clear that there will be any claims by the condominium corporation against the declarant that are not fully covered by the *ONHWP Act*. I do not accept this argument. The parties are now addressing alleged defects in the construction. The applicant is entitled to know the scope of its potential rights against the declarant. The impugned documents provide that the applicant will be liable to indemnify the respondent for any action brought in violation of them. Given this provision, it is reasonable for the applicant to obtain a ruling on the validity of the impugned documents before it proceeds in violation of the plain wording of those documents.

Conclusion

[28] A developer of a condominium is entitled to limit its risk, in much the same way that a builder of new homes may do so. The only mechanism for implementing such a limitation in respect to the common elements in a manner consistent with the notice requirements under the *Condominium Act* is an agreement to this effect between the developer and the condominium corporation that is (a) disclosed in advance to prospective purchasers; and (b) is registered on title so that subsequent purchasers will have notice of it.

[29] There is nothing illegitimate about a developer seeking to limit its risk in this way, provided, of course, it does not seek to contract out of the statutory requirements of the *ONHWP Act*.

[30] In this case, the developer has sought to limit its liability to the statutory requirements of the *ONHWP Act*. Notice of this was provided to all prospective purchasers, and was registered on title to give notice to any affected person including subsequent purchasers.

[31] The Province has instituted minimum standards for warranties applicable to new condominium construction. Those minimums are contained in the*ONHWP Act* legislation. There would be no need for those provisions if the effect of the *Condominium Act* is to preclude any derogation from common law liability for the developer.

[32] The applicant did not challenge the by-law, on its own, on the basis that it should be able to amend or repeal it. And that is because derogation from the by-law will not avail the applicant if the agreement is unscathed. The agreement is unscathed. And so the application is dismissed. Nothing in this decision precludes the applicant from amending its by-laws.

Costs

[33] Costs are payable by the applicant to the respondent on a partial indemnity basis, fixed at $12,000, inclusive, payable within thirty days.

Delay in Rendering this Decision

[34] I regret the delay in delivering this decision. I have been on an extended medical absence following a heart attack in August 2012, a premature return to work in October to December 2012, and I have not yet been able to resume work full-time. Hence the delay.

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D.L. Corbett J.

DATED: September 23, 2013

[1] *Rosen* v. *Grey Condominium Corporation No. 31* (unreported July 12, 2012, Ontario Superior Court, per Tulloch J., as he then was) concerns the jurisdiction (or lack thereof) of a condominium corporation to control the use made of individual units by unitholders (specifically, precluding short-term rental of units). *York Condominium Corp. No. 42* v. *Melanson* 1975 CanLII 352 (ON CA), (1975), 9 O.R. (2d) 116, 59 D.L.R. (3d) 524 (C.A.), per Howland J.A. (as he then was), concerns an absolute prohibition on all animals, a prohibition which is found to be overbroad and *ultra vires* by excessively limiting the unitholders' control and enjoyment of their own units. In *York Condominium Corporation No. 400* v. *Comcraft* Services Ltd. et al. (1988) 1 R.P.R. (2d) 301 (Ont. Dist. Ct.), per Davidson D.C.J., the court found that an age restriction on residents of the condominiums was *ultra vires* the board because the age restriction was not included in the declaration of the condominium. In *Basmadjian* v. *York Condominium Corp. No. 52* 1981 CanLII 1759 (ON SC), (1981), 21 R.P.R. 111, 32 O.R. (2d) 523, 122 D.L.R. (3d) 117 (Ont. H.C.J.) per Maloney J., the court considered that a fee imposed on unitholders who rent out their units was not the proper subject-matter of a rule or by-law, but rather would have to be included in the declaration to be effective.

[2] *Peel Condominium Corp. No. 41* v. *Tedley Homes Ltd.* 1997 CanLII 1585 (ON CA), (1997), 35 O.R. (3d) 257 (C.A.). See also *Metropolitan Toronto Condominium Corp. No. 1272* v.*Beach Developments (Phase II) Corp.*, [2010] O.J. No. 5025 (S.C.J.), per Penny J.

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