Ontario Real Estate Law Developments

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BUYER CAN'T RELY ON SELLER'S ENVIRONMENTAL REPORTS

— Jennifer Kalnins Temple, Saxe Law Office.

A recent decision out of Newfoundland should remind prospective purchasers of real estate NOT to count on Environmental Site Assessments (ESAs) or other environmental reports commissioned by the seller, unless they acquire a specific contractual right to rely on that report, e.g. through a reliance letter. Real estate lawyers, take note, please.

In *Community Mental Health Initiative Inc. v. Summit Lounge Ltd.*, 2014 CanLII 63978 (NL SCTD), the plaintiff, CMHI, entered into a purchase agreement to buy property from the defendant, Summit. The purchase agreement required Summit to provide CMHI with a Phase I Environmental Site Assessment in order to demonstrate that the property was free from contamination. The vendor hired a well known environmental consultant, Stantec, to conduct the ESA. Stantec issued a report concluding there were no grounds for concern. The seller provided the ESA to the buyer who then completed the real estate transaction. The buyer subsequently found hydrocarbons on the property. The buyer sued Stantec claiming that its Phase I ESA report contained misstatements and wrong information.

Stantec successfully filed a summary trial application to have the claim dismissed, arguing that it only provided the ESA for use by the seller, and it had no privity of contract with the buyer.

Disclaimers Work

The court referred to the following provision in the Agreement of Purchase and Sale:

> "Vendor will provide Purchaser with a Phase 1 Environmental Site Assessment, at Vendor's cost, verifying that the property is free of any potential or actual environmental contamination . . ."

The court also referred to this standard provision from the Scope of Services Agreement entered into between the seller and Stantec:

> "Third Party Reliance: Only the Client shall be entitled to rely on the Documents provided . . . in the performance of the Services. The Documents relate solely to the Services for which [Stantec] has been retained and shall not be used or relied upon by the Client or any third party for any variation or extension of the Services, any other project or any other purpose. Any unpermitted use by the Client or any third party is strictly prohibited."

Finally, the court referred to the following statement in the final Phase I ESA report:

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> "7.0 Closure: This report has been prepared for the sole benefit of [the seller]. The report may not be used by any other person or entity without the express written consent of [the seller and the contractor]. All parties are subject to the same limit of liability as agreed to in the contract under which the work was completed. Any use which a third party makes of this report, or any reliance on decisions made based on it, are the responsibility of such third parties. [The contractor] accepts no responsibility for damages, if any suffered by any third party as a result of decisions made or actions taken based on this report."

These clauses are found in essentially all environmental consultant's reports in Canada.

The Court held that Stantec owed no duty of care to the buyer. Referring to the U.K. House of Lords decision *Hedley Byrne & Co. v. Heller & Partners*, [1964] A.C. 465 (H.L.), the principles of which were applied by the Supreme Court of Canada in *Edgewood Construction Limited v. N.D. Lee Associates*, [1993] 3 S.C.R. 206, the court held that a duty of care will not arise when, in the contract, the defendant employs specific language disclaiming such a duty.

Why don't real estate lawyers know about environmental reliance letters?

This result should not have been a surprise. Environmental lawyers know that this principle was established nearly twenty years ago by the Ontario Court of Appeal in *Wolverine Tube (Canada) Inc. v. Noranda Metal Industries Ltd.*, [1995] 26 O.R. (3d) 577. There, an environmental consultant prepared a Phase 1 ESA for three of his client's properties. The Ontario Court of Appeal found that a subsequent purchaser could not maintain a claim in negligence against the consultant in light of a disclaimer clause which negated any duty of care to the purchaser. That is exactly what reliance letters are for.

Nearly twenty years after *Wolverine Tube*, why don't real estate buyers ask for a reliance letter? (Not that a Phase 1 guarantees anything anyway.) Why do so many buyers continue to believe that they are "entitled" to receive a clean site? And why don't real estate lawyers disabuse them of this dangerous and expensive notion?

Jennifer Kalnins Temple recently returned to Canada after spending over a decade litigating environmental issues in the United States. After graduating from University of Toronto Law School in 2002, she became an associate at an international law firm, McDermott Will & Emery LLPin their Manhattan office. She represented Fortune 500 companies involved in complex litigation relating to products liability, mass torts, and environmental laws. She has both jury and bench trial experience representing corporations, as well as not-for-profit associations.

STATE OF THE MORTGAGE MARKET IN CANADA

— Rose H. McConnell, LexisNexis.

The Canadian Association of Accredited Mortgage Professionals ("CAAMP") released its latest survey report, the Annual State of the Residential Mortgage Market in Canada (the "2014 Report").[1] The report provides insight into how Canadians are managing their mortgage debt. A significant consideration in reviewing this report is that since home equity is a large repository of wealth in Canada, trends in house prices can greatly influence the confidence of consumers and businesses. The report was compiled from information derived, in part, from an online survey of 2,000 Canadians. More than half of those surveyed were homeowners with mortgages. The rest were renters, homeowners without mortgages, and others who lived in circumstances where they were not required to make mortgage payments or pay rent.[2]

Mortgage Types and Amortization Periods

In regard to homes purchased during 2014, 84 per cent of respondents had mortgages, while four per cent did not have a mortgage, but did have a home equity line of credit ("HELOC"). The remaining 12 per cent had neither a mortgage nor a HELOC. For those homeowners with mortgages, fixed-rate mortgages were the most popular. In terms of amortization periods for those purchasing homes in 2014, 88 per cent had contracted amortization periods of 25 years or fewer, and 12 per cent had extended amortization periods.[3]

Debt Load of Mortgagors

Low interest rates in Canada have influenced housing activity. A previous report compiled by CAAMP in 2011[4] concluded that Canadian mortgage borrowers and lenders had the capacity to absorb higher interest rates. This was

based on the average gross debt service ("GDS") ratio and the total debt service ratio ("TDS") of Canadian borrowers.

The GDS is generally defined to be the percentage of borrower's income needed to pay all monthly housing costs, which include a mortgage, property taxes, heat, and 50 per cent of condominium fees, if applicable. It is calculated by lenders by adding up all of a borrower's monthly housing-related costs on an annual basis, and dividing the total by the borrower's total gross income, then multiplying the sum by 100.[5] The TDS is calculated by determining the percentage of a borrower's income that is needed to cover housing costs (the GDS) plus any other monthly obligations that an individual has, such as credit card payments or car payments.[6]

Even though the data used for the 2011 CAAMP report[7] concentrated on the highest risk mortgages, the results indicated that a majority of Canadian borrowers had left themselves considerable room to absorb interest rate increases.[8]

Mortgage Arrears

The 2014 Report referred to data provided by the Canadian Bankers Association which indicates that only a small percentage of Canadian mortgage holders are behind in their payments (here, "behind" means mortgages that are three or more months in arrears). The arrears rate is approximately one in 350 borrowers, or 0.29 per cent.[9]

Interest Rates

Based on the survey results, the average mortgage interest rate for current mortgage holders is 3.24 per cent, as of the fall of 2014. This is down from the rate seen in the fall of 2013, which was 3.5 per cent.[10] Interest rates vary depending on the type of mortgage (fixed rate versus variable/adjustable rate), with fixed rate mortgages generally having higher interest rates than that of variable/adjustable rate mortgages.[11]

An analysis carried out on surveys results complied for the 2011 report indicates that a majority of borrowers were in a position to afford increases in mortgage payments that would result from an increase in the interest rate to five per cent.[12]

The 2014 Report also notes that the average interest rate for a fixed rate mortgage is 3.36 per cent, which is below the typical posted rates that have been available during 2014. Since the beginning of 2014, the posted rates for five-year term mortgages have averaged 4.91 per cent, indicating that "there is a substantial amount of discounting in the mortgage market".[13]

Housing Market Outlook

During the past 20 years, the rate of mortgage credit growth in Canada has varied, from five per cent per year in the mid-1990s to a peak of 10 per cent from 2004 to 2008 and more recently, back to five per cent per year. Following are some factors that may influence an increase or decrease in the growth rate of mortgage credit:[14]

- A movement by Canadians away from slow growth communities into communities with stronger job markets, which also have higher house prices and, consequently, larger associated mortgages;
- The completion of new homes;
- Low interest rates which could result in borrowers having more money available to repay their mortgage principle amounts, which would tend to reduce the rate of mortgage growth; and
- Trends in the resale housing market has less of an impact on the rate of mortgage credit growth because when a resale property is purchased and a mortgage obtained, an existing mortgage is often discharged, so the net impact is less important compared to the purchase of new homes.

The report comes to two key conclusions: (1) the negative impact of policy change is diminishing, but continues to influence housing activity; and (2) there is a wide divergence regarding housing indicators across the country — in many areas of Canada housing markets are weak.[15]

Notes:

[1] Will Dunning, *Annual State of the Residential Mortgage Market in Canada*, 2014, Canadian Association of Accredited Mortgage Professionals, http://www.caamp.org/meloncms/media/Annual%20State%20Report%20Fall%202014.pdf (accessed on December 4, 2014), p. 3.

[2] *Ibid.*

[3] *Ibid.*, p. 4.

[4] At http://caamp.org/meloncms/media/Revisiting%20Cdn%20Mortgage%20Mkt%20Booklet.pdf (accessed on December 4, 2014).

[5] See, for example, http://www.whichmortgage.ca/article/what-are-tds-and-gds-ratios-174913.aspx (accessed December 4, 2014).

[6] See, for example, http://www.canadianmortgagetrends.com/canadian_mortgage_trends/2009/06/debt-ratios-gds-tds-ratios.html (accessed on December 4, 2014).

[7] See note 4.

[8] *Ibid.*, p. 1.

[9] See note 1 at p. 16.
[10] *Ibid.*, p. 18.
[11] *Ibid.*
[12] *Ibid.*, p. 19.
[13] *Ibid.*, p. 21.
[14] *Ibid.*, p. 32.
[15] *Ibid.*, p. 33.

RECENT CASES

Subcontractor's General Lien Holder Rights Extinguished

Ontario Divisional Court, October 8, 2014

The respondent, Nortown Plumbing (1998) Ltd. ("Nortown"), was a contractor for plumbing services for new homes in two residential subdivisions, one of which was owned by the respondent Burl 9 Developments Limited and the other by the respondent IntraCorp Projects (Milton on the Escarpment) Ltd. ("IntraCorp"). The appellant, Yorkwest Plumbing Supply Inc. ("Yorkwest"), was a subcontractor to Nortown in both subdivisions. The contracts between the contractor and subdivision owners provided that claims for liens pursuant to the *Construction Lien Act* (the "Act") would arise and expire on a lot-by-lot basis. In January 2012, Nortown made an assignment in favour of its creditors and a receiver was appointed. Yorkwest registered a claim for the entire sum it was owed by Nortown against each unsold lot in both subdivisions but did not register lot-by-lot liens. IntraCorp vacated Yorkwest's claim by paying approximately $60,000 into court. A motions judge granted summary judgment in the respondents' favour. He found that the general lien claim should be entirely discharged and the respondents' money returned to them on the basis of the lot-by-lot term in the contracts, which made it impossible for a general lien to arise. The appellant appealed.

The appeal was dismissed. Section 20(2) of the Act provides that no general lien arises "under or in respect of a contract that provides in writing that liens shall arise and expire on a lot-by-lot basis." The section makes no reference to a subcontract, only a contract. The Court considered the appellant's argument that the Act's intention was to exclude subcontracts from the exception and thus grant a subcontractor an independent right to a general lien that cannot be waived and that is unaffected by the contract between the property owner and its contractor. The Court found that the Act does not support the appellant's interpretation.

The Court noted that, pursuant to the Act, a claim for lien is secured to the extent of the holdback retained by each person paying money pursuant to a contract or subcontract. The Court noted that, if the appellant's position was correct, the property owner could not release the holdback to a contractor on a lot-by-lot basis, as an unpaid subcontractor could then register a general lien on any unsold lots for an amount equal to what remained unpaid for services supplied to all lots. Furthermore, under the appellant's interpretation, only the contractor could give up general lien holder rights and the contractor's surrender of those rights was virtually ineffective. Instead, the legislature could have simply stated that subcontractors have a right to a general lien and could rely upon section 4 of the Act to preserve it. The Court concluded that the respondents' interpretation had the benefit of certainty and did not eliminate the subcontractor's lien rights, but rather rendered them specific and required them to be preserved on a lot-by-lot basis. The Court concluded that when a contract between a property owner and contractor contains a lot-by-lot lien term, section 20(2) of the Act extinguishes all general lien holder rights for the contractor and all subcontractors. The Court further found that, based on section 55(1) of the Act, the appellant's claims for unjust enrichment and *quantum meruit* could not be joined with its lien claim.

Yorkwest Plumbing Supply Inc. v. Nortown Plumbing (1998) Ltd., 2014 OREG ¶59,069

Landlord and Tenant Board's Interpretation of Time Limitation Unreasonable

Ontario Divisional Court, October 8, 2014

The appellant tenants vacated their residential unit on August 31, 2012. On September 3, 2013, they brought an application under section 57(1) of the *Residential Tenancies Act, 2006* (the "Act") alleging that the respondent landlord had given them a notice of termination of their tenancy in bad faith. The Landlord and Tenant Board (the "Board") dismissed the application as untimely. Pursuant to section 57(2) of the Act, bad faith applications cannot be made

more than one year after the former tenant vacated the rental unit. The one-year anniversary date of the tenants' vacating the unit fell during the Labour Day weekend and the appellants filed their application on the first business day after that weekend. The Board held that section 57(2) of the Act provides a limitation period for the filing of a bad faith application and the Board has no power to extend or shorten the period, pursuant to section 56(2) of Ontario Regulation 516/06 (the "Regulation") under the Act. The appellant tenants appealed from the Board's order and review order.

The appeal was allowed. The Court found that the Board was not being asked to extend the time limit but to compute the time limit required under section 57(2) of the Act. The Act required that the time be calculated in accordance with the Board's Rules of Practice under the Act. Rule 4.3 states that if the time limit for filing a notice or document falls on a non-business day, the notice or document can be filed on the next business day. There was no support for the Board's finding that Rule 4.3 did not apply to section 57(1) applications, the Court found. "Notice or document" included applications. It was unreasonable to interpret the Act so as to effectively shorten the tenants' time limit for filing their application and requiring them to file it before the holiday weekend. The Board also unreasonably interpreted section 89 of the *Legislation Act, 2006* as not applying to the Act. Section 89, along with Rule 4.3, in fact served to make parties aware of time limitations for circumstances that involved days when business offices are closed. Having regard to the above, the Court set aside the Board's orders and remitted the application to the Board for a hearing on the merits of the application.

Ashford v. Johnson, 2014 OREG ¶59,070

Court Upheld Condominium Corporation's Bylaw Limiting Declarant's Liability for Warranty Issues

Ontario Court of Appeal, October 22, 2014

The respondent, West Harbour (I) Residences Corp., was the declarant of the appellant condominium corporation registered as Toronto Standard Condominium Corporation No. 2095. The appellant's first board of directors, which was elected by the respondent, adopted a bylaw requiring the appellant to enter into a warranty agreement with the respondent under which the respondent's warranties in respect of the common elements of the condominium were limited to the statutory warranties in the *Ontario New Home Warranties Plan Act*. The agreement further prevented the appellant from making any warranty claims in respect of the common elements except through the Tarion Warranty Corporation process.

The appellant's new board of directors, elected by the unit owners, brought an application seeking a declaration that the bylaw and agreement were invalid, because enacting the bylaw and entering into the warranty agreement were beyond the authority of the first board of directors. Further, the appellant alleged that the bylaw and agreement were unreasonable and inconsistent with the *Condominium Act, 1998* (the "Act"). An application judge dismissed the appellant's application, finding that no legislation limited a developer's ability to limit its liability in respect to common elements. The appellant appealed.

The appeal was dismissed. Pursuant to section 56(1) of the Act, a board may make bylaws to, among other things, govern the management of the property; govern the use and management of the assets of the corporation; specify duties of the corporation in addition to the duties set out in the Act and the declaration; and govern the conduct generally of the affairs of the corporation. The Court accepted the appellant's argument that the provisions were "general"; however, the appellant did not provide any case law to support its position that the power granted in the Act should be ignored or read down because of this generality. The Court found that the board's decision to limit the corporation's options in making claims against the developer was an exercise in the governance of the affairs of the corporation and was authorized by section 56(1)(*p*). The Court dismissed the appellant's argument that, because the bylaw disposed of the right to sue the respondent for construction deficiencies, it impaired the appellant's ability to meet its repair and maintenance obligations under the Act.

The Court further found that section 23, which provides the condominium the power to make claims, was not violated, as it simply provides that a condominium corporation "may" commence a claim for damage to common elements with no statutory requirement that a claim be made. The Court dismissed the appellant's argument that the board of directors breached its statutory obligations under section 37(1). The appellant cited no case in which section 37(1) formed the basis for a finding that a particular bylaw of a condominium board was *ultra vires*. The bylaw and agreement were also found not to be unreasonable, pursuant to sections 56(6) and (7) of the Act. The Court dismissed

the appellant's argument that consideration and disclosure under the bylaw and agreement rendered it unreasonable. The Court concluded that the bylaw and agreement were lawful and valid.

Toronto Standard Condo. Corp. No. 2095 v. West Harbour City (I) Residences Corp., 2014 OREG ¶59,071

Encroachment Onto Right of Way Not Actionable

Ontario Court of Appeal, October 24, 2014

The parties owned contiguous properties in a development in Toronto, comprised of six row houses that backed onto a laneway where a garage for each house was located. The laneway was accessed via an entrance from the street. The respondents constructed a large addition to their house. Part of the addition encroached on the land that was subject to the right-of-way. The deeds of the appellants indicated that they were granted a right-of-way over Part 19 on the development's registered plan for the purpose of vehicular access. Part 19 was the part of the respondents' property that was subject to the right-of-way. The encroachment of the addition reduced the passable portion of Part 19, however, it was still possible to enter the laneway with a large vehicle. The appellants took the position that the addition amounted to a real and substantial interference to their right-of-way and sought a declaration that the respondents' conduct was a violation of their rights.

An application judge found there was no actionable encroachment, because it did not create a real or substantial interference with the use of the laneway for vehicular access. The appellants appealed, arguing that they had a right to use the entire right-of-way and that the encroachment was actionable even if it did not interfere with the appellants' ability to use the right-of-way for the purpose identified in the deed. The appellants did not challenge the application judge's finding that the laneway "remains as accessible and passable now as it was before the construction."

The appeal was dismissed. The Court agreed with the application judge's finding that, pursuant to the authorities, "an encroachment on a private right-of-way is actionable only where the encroachment substantially interferes with the dominant owner's ability to use the right-of-way for a purpose identified in the grant". The Court noted that this requirement reflects the nature of the dominant owner's right — namely, that he or she does not own the right-of-way but only enjoys the reasonable use of the servient owner's property for its granted purpose. To make a finding, a court must have regard to the terms of the grant and the nature of the encroachment and determine the significance of an encroachment, depending on its impact on reasonable use. There was no supporting case law for the appellants' argument that an encroachment by a permanent structure is a substantial interference, whether or not the encroachment actually interferes with the dominant owner's reasonable use. Considering the application judge's factual findings and the fact that the appellant accepted the finding regarding the laneway remaining passable, the Court dismissed the appellants' appeal.

Weidelich v. De Koning, 2014 OREG ¶59,072

Broker Failed to Satisfy Condition Precedent in Listing Agreement

Ontario Court of Appeal, October 27, 2014

The appellant real estate investment firms, Elcarim Inc. and Elcarim E Legna Inc. (collectively "Elcarim"), and their director, Elaine Wai Mascall ("Mascall"), entered into a listing agreement (the "agreement") with the respondent, Ariston Realty Corp. ("Ariston"), for the sale of a property. Ariston was a real estate brokerage firm at which the respondent, Anthony Philip Natale ("Natale"), was a principal. The agreement included a holdover clause which stated that a commission would be paid to Ariston on the completion of a sale to any party to whom Ariston introduced the property during the term of the agreement, provided Ariston notified Elcarim of the purchaser's name in writing prior to the expiry of the agreement. During the term of the agreement, Ariston introduced the eventual purchaser to Mascall; Ariston, however, never provided written notification that it had introduced the purchaser to the property. After the sale closed in April 2002, Elcarim refused to pay Ariston commission on the sale. Ariston commenced an action for payment. The trial judge held that Ariston's failure to provide written notice of the introduction was of no significance, and held Elcarim and Mascall personally liable for the unpaid commission. The appellants appealed. The respondent cross-appealed, seeking compensation under the doctrine of *quantum meruit*.

The appeal was allowed and the cross-appeal was allowed in part. The Court found that the trial judge effectively replaced the requirement of written notice with a requirement of actual notice by interpreting the holdover clause as requiring that Elcarim be made aware that Ariston introduced the eventual purchaser, regardless of whether written

notice of the introduction was provided. The Court found this interpretation did not accord with sound commercial principles and good business sense, as the requirement of written notice was intended to promote commercial certainty and to reduce the potential for litigation. The Court concluded that the provision of written notice was a condition precedent to Ariston's entitlement to commission, and, having failed to fulfill the condition precedent, Ariston had no contractual entitlement to commission. The Court therefore dismissed Ariston's claim for commission. The Court further found that the trial judge had erred in finding Mascall personally liable, as the evidence did not establish that she had acted in pursuit of some interest separate from that of the corporations.

The Court found, however, that Ariston was entitled to compensation on the basis of *quantum meruit*. While Ariston could not claim its commission on the basis of *quantum meruit* for services provided during the term of the agreement, Ariston could claim reasonable compensation for the services provided after its expiry. The trial judge had found that Natale continued to assist Elcarim after the expiry of the agreement, and the Court valued these services at $20,000.

Ariston Realty Corp. v. Elcarim Inc., 2014 OREG ¶59,073

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For Wolters Kluwer CCH

Rose McConnell, BSc, LLB, Analyst
Law & Business
416-224-2224, ext. 6438
email: Rose.McConnell@wolterskluwer.com

Dionne Cheong, Marketing Manager
Law & Business
416-228-6153
email: Dionne.Cheong@wolterskluwer.com

Rita Mason, LLB, Director of Editorial
Law & Business
416-228-6128
email: Rita.Mason@wolterskluwer.com

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Wolters Kluwer Limited
300-90 Sheppard Avenue East
Toronto ON M2N 6X1
416 224 2248 · 1 800 268 4522 tel
416 224 2243 · 1 800 461 4131 fax
www.cch.ca