

LATHEM'S LEGALS

Real Estate Law Series of Newsletters

THE PURCHASE OF NEW CONDOMINIUMS IN ONTARIO

Over the last 20 years we have aided in the purchase of thousands of condos for our clients and the purpose of this newsletter is to provide an explanation of the standard form of a new condominium purchase contract. The purchaser of a new home from a builder registered with TARION in the Province of Ontario is generally a legal point of view a very safe purchase. The main risks associated with the purchase of a new home would relate specifically to overall market conditions.

It is important, however that a new home buyer understand many of the terms of a new home contract which are a reflection of fairly extensive Government Regulation. In addition it is always recommended that a lawyer whose practice area is in Real Estate and familiar with new home contracts review the contracts to ensure that they do follow the required format and to negotiate or itemize any additional costs.

While the purchase of a new home is subject to very similar regulations it is less complex and is dealt with in an additional newsletter. This paper is not adequate to deal with a new home purchase.

OVERALL REGULATORY FRAMEWORK

As mentioned the purchase of a new condominium is extensively regulated in Ontario. In fact, it is illegal to build a new condominium for sale to the public without being registered with TARION, which is a quasi Governmental Agency that administers the Ontario New Home Warranties Plan Act.

The 4 pieces of legislation that provide the overall regulatory framework for the regulation of the construction and sale of a new condominium to the public fall under 1 of 4 pieces of legislation:

1. Planning Act;
2. Building Code Act;
3. New Home Warranties Plan Act and
4. Condominium Act.

Planning Act

The Planning Act gives the local municipality the right to control the overall development of land within its borders and use. More specifically it gives it the right to approve and supervise the construction of the physical infrastructure of roads, water, sewer as well as impose capital taxes to build schools, roads, transit etc. It is normal practice in Ontario for the Municipalities to require the developer and/or builder to post bonds for the value of the construction of the infrastructure being built. This ranges from the cost of constructing to roads, water and sewer to the grading of individual lots.

The main protection the public and municipality has from a sketchy or insolvent builder is the bonds posted by the developer builder, which is usually equivalent to cost of the work to be done. The purpose of the bond is that if the developer does not comply with its obligations the municipality may make use of these financial guarantees so that homeowners do't become burdened with the obligations of a developer who has become bankrupt or breaches its agreements with the municipality.

This has less of a direct impact on the New Condominium buyer than a new home buyer because the infrastructure is usually built prior to the actual condominium itself. The financial guarantees, however ultimately protect the purchaser in the same way.

Building Code Act

The standard of construction of new condominium is dictated by the Building Code Act, which is administered by the local municipality. The act itself does essentially 3 things relevant to the new home building process:

1. It imposes the minimum construction standards for all buildings;
2. It imposes a regime of inspections to ensure that there is no cheating in the construction; and
3. It sets the standards for occupancy.

The standards for occupancy are important because the New Home Warranties Plan Act, dictates that the buyer must move into the home if it is unfinished once the builder can obtain a occupancy permit. So the Municipality utilizing the standards of the Building Code Act, is the neutral 3rd party that determines when the purchaser may require the builder to close.

New Home Warranties Plan Act

The New Home Warranties Plan Act, is administered by a quasi governmental agency known as TARION. By in large TARION stands as a financial guarantor of the builder's financial obligations and quality of the construction in the event of default.

The TARION regulations cover 3 areas:

1. Extension of closing dates;
2. Guarantee of the deposits; and
3. Guarantee of the construction.

Again the main object is to protect the buyer from a insolvent or perhaps dishonest builder. By being the Guarantor TARION sets the rules in the contract between the builder and new home buyer as they relate to extensions, deposits and defects in construction. So generally these provision of the contract are standard and cannot be changed.

What Tarion does is guarantee the following:

1. That if the builder does not follow the proper extension rules and penalties are triggered, that if the builder refuses to pay them, TARION will do so.
2. TARION guarantees the deposits paid by a home owner to a builder, should the builder go bankrupt prior to the title transfer up to \$20,000.00. Any deposits in excess of \$20,000.00

are not ensured through TARION, however, the condominium act requires that any amounts over \$20,000.00 be insured through excess deposit insurance.

3. TARION guarantees the quality of the construction against physical defects. All items are guaranteed against defects for 1 year. The mechanical systems are guaranteed for 2 years and the structure, foundation and water penetration is guaranteed for 7 years. In return for this guarantees TARION is the organization that determines what is a defect and the homeowners right to compensation. This means that if there is a dispute for any of the above issues generally a buyer cannot go to Court but must go through a complaint and arbitration process setup by TARION.

Condominium Act

The Condominium Act has provisions in it that deal with the selling, construction and occupation of new condominium, as well as the ongoing governance and management of existing condominiums. They set rules of the occupancy of the building prior to the ownership transfer as was to the interest paid on deposits and interest paid on the balance due on closing, as well as the handling of the deposits over \$20,000.00. The requirement is that any deposits in excess of \$20,000.00 must be insured by the builder's lawyers prior to them being released to protect the buyer against bankruptcy of the builder.

Role of Title Insurance

While not officially part of the regulatory regime, Title Insurance is used in virtually every Real Estate Transaction in Ontario. Where title insurance comes in, is that it also guarantees where it is used that there has been compliance with the Subdivisions Agreements between the developer and municipality and guarantees that the bonds are in place. This in effect adds another layer of protection to the buyer.

EXTENSION PROVISIONS

All TARION contracts permit the builder to extend the closing date. In return they impose a penalty on the builder if the builder does not give proper notices of the change in closing date. The penalty structure and how compensation is determined has been changed over the years and it is best to consult with TARION regarding specific entitlements. Claims must be made currently within six (6) months of closing.

The current requirements are that the builder may delay the closing date from the earliest one set up in the TARION schedule in every contract to the latest one, based on at least 90 days prior notice to any date previously set. Once the last date in the contract period is reached the buyer has a right to cancel the contract, providing he gives notice within 30 days.

There are also are typically conditions in the contract that allow the builder to cancel the contract if they are unable to build the house as specified.

My experience is that in the GTA there are usually substantial delays in the closing date, however, typically most builders comply with the notice provisions and while I would suggest a quick call to the builder most people are safe to consider selling their homes or giving notice once they are less then 90 days from a set closing date.

INTERIM OCCUPANCY AND OCCUPANCY FEES

This concept is unique to the purchaser of condominiums and falls under the Condominium Act. Due to the fact that the surveys that create title can only be completed after the building is fully constructed the building is usually ready for occupancy approximately 6 to 9 months prior to when title can be transferred. This period is called the occupancy period and is a result of completing the survey, drawings and obtaining approval for their filing at the Land Registry Office by the local municipality and land registrar.

The builder must give 90 days prior notice to the occupancy date in order to delay the occupancy from the date first set out in the agreement. Any subsequent delays must also be done on 90 days notice. At occupancy the buyer is required to move in and pay an occupancy fee to the builder. The amount of the occupancy fee is regulated by the Government and consists of an monthly fee made out of 3 items:

1. An estimate of the annual property tax divided into monthly payments;
2. The monthly maintenance (condominium or common expense fee); and
3. Interest on the amount of the unpaid balance of purchase price at an amount set by Government Regulation which currently is the same as a 1 year open mortgage.

This fee is paid until the title transfer date, at which point the occupancy fee, taxes and condominium fees are adjusted and the balance of the purchase price plus any other charges owing are paid to the builder. The title transfer date as mentioned above is typically 6 to 9 months from the occupancy date with 30 days advance notice normally given to the owner.

While 6 to 9 months is the norm and anything beyond 1 year is unusual this period can legally run for up to 2 years.

UNFINISHED HOMES PROVISIONS

TARION regulations and all new condominium contracts essentially provide that the buyer will complete the closing of a new condominium purchase once the builder has obtained an occupancy permit. The standards for the occupancy permits are set out in the Building Code Act. This in turn is policed by the local municipality.

TARION itself guarantees that the items unfinished at the time of closing will be finished. The PDI (Pre-Delivery Inspection) and the schedule of incomplete or damaged items forms the list that TARION is guaranteeing.

The buyer is not permitted to refuse to close or hold back funds for unfinished items, but is required to rely on the TARION guarantee. There are also other implications for the buyer holding back funds under the Construction Lien Act, which are relevant.

TARION itself then becomes the Guarantor and Arbitrator of the process of determining what is a deficiency and whether the builder has completed its obligations. Should the builder refuse then TARION will step in and complete any required repairs.

TYPICAL CONSTRUCTION VARIATIONS ALLOWED BY THE CONTRACT

Do to the fact that most new homes are sold prior to complete approval by the City the contract itself allows for typical variations in the following:

1. Size of the unit up to 5% typically;
2. Can be built in mirror image to the plans; and
3. Minor variations in the layout

The contract itself will allow for a certain variation in the overall condominium building including number of floors, commercial units and so forth.

EXTRA COSTS

The main provisions of a new condominium contract that the buyer's lawyer can request changes is in the additional costs. Typically new homes are sold at a specific price, with the builder passing on specific costs to the buyer. Typically the builder tries to pass onto a buyer the costs that are required by legislation to be borne by the buyer, such as the TARION warranty fee itself.

There are other costs which change over time and the builder often tries to have the buyer absorb. They include, the municipal levies or increase in levies, costs for the utilities and hookups, reserve fund contributions, charges of the builder's lawyers such as Law Society Levies, Fees for preparing transfers.

The main role of the lawyer is to be able to identify and if possible estimate for the buyer what these additional costs are. Also the lawyer will normally try to eliminate some of the costs, or to have them at least specified or capped.

Currently the average extra charges that we see on a home range from \$6,000.00 to \$8,000.00. The big items that a buyer needs to look out for are the increase in levies and development charges.

HST REQUIREMENTS

HST is applicable in the sale of all new condominium and it is not as simple as "its included". Condominiums are sold to buyers on the assumption that they will move into it as their principal residence. So it is included "net of rebates", or at a reduced amount of HST. Where the buyer does not qualify because they are not purchasing it as a "primary residence" for themselves or an immediate family member the builder must collect the full amount of HST and remit it to CRA.

A simple rule of thumb is that the "discount" in HST is approximately 8%, below \$450,000.00, or a flat \$24,000.00 over \$450,000.00. So if the person does not qualify and the purchase price is under \$450,000.00, I would recommend using 8% as a rough estimate. If it is over \$450,000.00 it is \$24,000.00. These are not exact figures.

The other HST rules that one needs to be aware of is:

1. If the property is a rental, the additional HST will be returned by CRA if within 1 year of closing the buyer submits an application with proof that it was a rental property including a 1 year lease.
2. The “primary residence” requirement does permit additional personal use properties, so in theory secondary residences such as weekend or vacation homes do not qualify.
3. Properties that are flipped are typically not entitled to rebates, meaning that even rental properties sold within 1 year do not qualify.

MISCELLANEOUS CONDOMINIUM SPECIFIC ISSUES

The biggest issue that arises in the purchase of new condominiums is the builders estimate of the maintenance fees etc. My honest opinion is that they are arrived at with sales in mind and are typically not that accurate. By in large condominiums are completed often years after the builder originally estimates. In return this gives the builder great leeway in not being accountable for deliberately low estimates, which the builder can claim are the result of inflation.

Also, the maintenance fees are often set so low that when the Reserve Fund Study is completed it almost shows that the reserve is significantly underfunded. This study is rarely completed in the 1st year of the condominium when the builder is responsible for any shortfalls in the budget, but must be completed before the 3rd anniversary. It is not unusual to see contributions have to rise 20% for a period of 5 years following the completion of the study.

When it comes to the condominium fees on a new condo my best advice is if it looks too good to be true it usually is. What we find is that these fees usually rise to fall in line with other condominiums that may be 10 or more years old. I view most of the builder’s estimates of condominium fees as unreliable. I would also say because of the extent of delay in construction its an area in which builders are difficult to be held to account.

Bottom line is that I would assume that the Condominium fees in the long run will turn out to be similar to any building covering similar costs. There are no savings in buying a new condominium from this perspective.

SUMMARY

New Condominium Regulations do a lot to protect a buyer against the big risks of buying a new condominium. What the regulations do not do well is to protect a buyer against the small problems.

RESOURCES

The best resource I can recommend for new homes is the TARION website. On the website it contains a more detailed breakdown, as well as contact information for more detailed inquiries on TARION issues.

<http://www.tarion.com/>

I can recommend our firm website for resources:

www.lathemlaw.com

We also have a Youtube Website covering many of these same topics.

<https://www.youtube.com/channel/UCh4ob4Ez3juWpypYI9KX1yA>

CRA July 2011 Bulletin on HST and Assignment Contracts

<http://www.cra-arc.gc.ca/E/pub/gi/gi-120/gi-120-e.pdf>

The Law Society of Upper Canada

https://www.youtube.com/watch?v=AB_KwRCX5qw