



photo: Dianne Werbicki

First-year boards face a number of issues including turnover and construction deficiencies. A condominium development on King Street in Waterloo, Ontario.

Condo Board ABCs

Achieving Balance and Cooperation

By John A.A. Deacon

- How often does a condominium board of directors have to make a decision when there are very good reasons to decide in the negative and apparently just as good reasons to decide in the positive?



- How often does a condominium board of directors try to clarify a position by retaining an expert (engineer, lawyer) only to realize further implications of an issue and require further thought, discussion and debate?

- How often is a condominium board of directors accused of acting

too slowly, indecisively, and not representing the owners' best interests?

While it is clearly a benefit to a property administration to have a board of directors that can act quickly and decisively, it is perhaps even more critical that the board of directors act in a manner where all aspects of a decision are fully disclosed, considered and debated. Diversity of opinion among directors is a good thing provided it is heard, respected and considered in making a decision. Once the decision is made by the board, the condominium corporation has acted and committed, and all directors should move cooperatively with management to implement the decision.

The final, and many believe most important, aspects of decision-making are the recording and communication of the consideration, the decision and the impact of the decision on the community of owners and residents. Thus, minutes indicating all aspects of the decision considered by the board should be recorded. Stakeholders (the unit owners) should be informed of the authority of the board to make the decision, the board's considerations and actions, and the relevant timing, cost and impact of implementation.

In the balance of this article, a number of issues facing new condominium boards will be highlighted.

It is well-known that there is a

substantial burden on newly elected directors in the first year of a condominium corporation, including dealing with turnover issues, handling construction deficiencies, arranging and complying with the first reserve fund study, terminating contracts pursuant to s. 112 of the *Condominium Act, 1998* (hereinafter referred to as the “Act”) and many other matters.

However, this article will focus on issues facing such newly elected directors in the second year of opera-

tion of a condominium corporation when such directors can anticipate intense scrutiny by owners. This scrutiny will result not only from the importance of such decisions, but the very substantial impact on the common expenses. Two of these second year issues are highlighted in this article: 1. pursuing outstanding claims against the declarant, relating both to the operating deficit guarantee, and resolving construction deficiencies, and 2. insuring the adequacy of the reserve fund.

■ The First Year Operating Deficit

While it is great that a declarant must promptly pay a first year operating deficit, this consumer protection provision of the Act contains serious drawbacks.

- Because developers compete with other condominium projects for unit sales and comparisons are based on per square foot costs and estimated budgets, common expenses are often underestimated to unit purchasers.

- Because of unclear wording in the Act, condominium declarants believe they are free to underestimate the first year reserve fund contribution (for which they are partly responsible) by pegging it at 10% (despite the well documented realistic range of between 20–30% of the operating budget.)

- While the declarant must pay the deficit within 30 days of its receipt of the audited financial statement, this is a rare occurrence.

- Unit owners who have budgeted their personal expenditures based on the representation in the first year budget statement are in for a very rude shock in the second year when actual costs are not buffered by any declarant deficit responsibility.

Looking at the condominium board ABCs, clearly advice will be needed from management, the corporation’s auditor, and often the corporation’s lawyer. The board will obtain advice concerning the ability of the declarant to pay the deficit, items in the deficit calculation that may be challenged and the costs and delays inevitable in pursuing such challenges. Yet ultimately the board must act decisively based on the best available information and due consideration of the consequences of its actions on owners and the common expenses.

Increasingly, excellent written resources are available for directors, including ACMO/CCI conference materials from the last two fall conferences, legal texts, case and statute law compendiums (such as Halsbury’s) and professional publications such as this journal.

The board’s most consistent resource is professional property management and directors should fully

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avail themselves of this resource to be fully informed of all implications of the issues involved, and whether further expert and/or professional advice is needed.

For example, a number of technicalities concerning the first year deficit are contained in the Act including the 30-day notice requirement in sub-section 75(5) triggering the declarant's obligation to pay. The board of directors should obtain advice relating to this 30-day period, its commencement date and notice delivery requirements. Similarly, if a declarant fails to pay, the board of directors must be aware of the two-year limitation period for commencement of action to collect the deficit. Ongoing negotiations concerning disputed aspects of the claim will not interrupt this limitation period except in very special circumstances. Mediation and arbitration of disputes is also mandatory under sub-section 132(3) of the Act but directors should obtain legal advice on timing of such proceedings, as the limitation period may still expire leaving the condo without

a remedy, and directors exposed to possible liability.

■ Correction of Construction Deficiencies

A condominium board of directors should consider creating or obtaining from management a checklist of issues to be considered and debated in achieving a satisfactory resolution of construction deficiencies within a reasonable time. This checklist should include:

- retaining a qualified person to conduct the performance audit;
- ensuring continuing contact with the declarant before, during and after completion of the performance audit;
- preserving Tarion remedies, if available;
- preserving legal remedies – advice on limitation period issue;
- structuring a settlement to ensure adequate deficiency correction – especially serious implications of release documentation; and
- ensuring the need for updated

performance audit completion reports should progress stall.

The above headings are by no means comprehensive, and each subject includes numerous other issues about which directors should inform themselves with suitable professional advice.

■ Reserve Fund Issues

The board of directors elected upon or after turnover from declarant control can take unfair blame for the shock experienced by unit owners over the typical 20–40% increase in owner common expense contributions in the second year. If, as is common, the declarant selects 10% of the operating budget as the contribution to the reserve fund, there will be a major financial issue in the second year.

Unfortunately this article cannot be conclusive on appropriate action by a board to obtain a remedy for this heavy financial burden on the unit owners because court cases have yet to be decided concerning whether the first year deficit remedy is applicable



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to reserve fund under-contribution. As well, a legislative initiative is currently being pursued with the Ontario government to define "adequacy" of a reserve fund and the appropriate disclosure budget reserve fund contribution amount.

To avoid unfair blame, a board of directors must use every opportunity to communicate clearly and transparently with owners. While litigation advice and issues are confidential, owners must be made aware at the earliest opportunity of mounting deficits, reserve fund studies, anticipated shortfalls, deadlines to attain adequacy, involvement of the corporation auditor, reserve fund studies and legal counsel in ensuring all appropriate steps are taken to

protect owners' interests. Communication to owners can include a regular newsletter, information meetings, social events, direct correspondence and consistent updates all explaining the issue, the potential impact, the advice received by the board and the board's actions to achieve balance and cooperation.

■ Conclusion

It is my personal view that the proper handling of first and second year issues by the homeowner elected board will set a course of clear sailing for the future financial security of the condominium corporation.

If these issues are not handled well, an atmosphere of mistrust, frustration and anger can set a con-

dominium corporation on a negative course with a significant negative impact on individual owners, the community and property values.

Year two directors should accordingly go to great length to deal correctly with governance issues, such as exercise of due diligence by directors (the ABCs) as mentioned in this article and other publications including preparation by directors for board meetings, full and informed debate, adequate record keeping, transparency and communication, and avoidance of conflict of interest. ■

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