

# About Condo

## **OBLIGATIONS AND LIABILITIES OF A CONDOMINIUM CORPORATION AND ITS BOARD OF DIRECTORS**

*The duties and obligations of condominium corporations and their boards of directors are real and serious legal obligations. Unit owners electing, or seeking to be elected to, a board of directors, may benefit from an understanding of those basic duties and obligations. Recently, we were asked to prepare a brief outline of the same for the general information of unit owners of one of our clients at the time of election of directors. This memorandum is adapted from that document.*

*This memorandum is not an extensive analysis of condominium or board obligations or the relevant provisions of the Condominium Act, 1998. It sets out the basics that every director and unit owner should understand about the essential duties and liabilities that hang over every condominium corporation. For detailed analysis of particular cases or concerns, the reader should consult legal counsel directly.*

### **CONDOMINIUM CORPORATIONS**

Condominium corporations are legal entities that are ‘creatures of statute’. As such, they have only those legal objects, rights, duties and powers that are granted to them by their governing statute, which, for condominiums in Ontario, is the *Condominium Act, 1998*.<sup>1</sup>

The condominium corporation (as well as every director and unit owner and resident) is required to comply with the Act, and the declaration, by-laws and rules of the corporation (s. 119(1)).

The condominium corporation has a statutory duty to “control, manage and administer the common elements and assets of the corporation” (s. 17(2)). In conjunction with this, the condominium corporation is required to repair all regular common elements of the corporation after damage (s. 89(1)). In addition, subject to the provisions of the declaration of the condominium, the condominium corporation is responsible for maintenance and repair of the common elements and repair after damage of the units (s. 89(1), 90(1) and 91).<sup>2</sup>

The corporation cannot neglect its duty to care for the property of the condominium without being in breach of its governing law.

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<sup>1</sup> All statutory references in this memorandum are to the *Condominium Act, 1998* unless otherwise indicated. All references to “the Act” mean the *Condominium Act, 1998*.

<sup>2</sup> The declaration of the corporation may alter these obligations. The obligation to repair the common elements after damage, however, cannot be changed.

## CONDOMINIUM BOARDS OF DIRECTORS

### **General**

The powers, duties and functions of the board of directors (“board”) of a condominium corporation are also set out in and governed by the *Condominium Act, 1998*.

The board of directors is to manage the affairs of the corporation (s. 27(1)). Accordingly, the duties of the board are to the corporation as a whole and not to the individual unit owners. The board must ensure that the corporation carries out its duties in accordance with its objects that are defined by the Act.

The majority of work performed by the board of directors is to be done without necessity of seeking direction from or approval by the unit owners.<sup>3</sup>

This does not mean that the board is not ultimately accountable to the unit owners (they always have the power of remove and replace the directors, and that statutory right to demand that the board comply with the *Condominium Act, 1998*, and other governing documents, by court order if necessary), but it does mean that the board is expected to carry out its obligations in an independent and authoritative manner in accordance with applicable law defining the scope and purposes of the same.

The board is ultimately responsible for its decisions and should neither fetter nor derogate from its responsibility. Likewise, while in the best condominiums unit owners take active interest in the goings-on and operation of the corporation, they should not seek to micromanage or assume or undermine the authority of the board that is seeking to carry out its duties in accordance with applicable law.

All business of the corporation is to be conducted through board meetings at which a quorum of the board is present (s. 32(1)).

### **Standard of Care**

A corporate director is a “fiduciary”. Fiduciary obligations import requirements to loyal and honest fulfillment of duties and compliance with relevant law.

Pursuant to the Act, each director of a condominium corporation in Ontario must carry out his or her duties in accordance with the statutory standard of care (in addition to applicable principles of common law); namely, to (s. 37(3)):

- (a) *act honestly and in good faith; and*
- (b) *exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.*

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<sup>3</sup> This is the point most commonly misunderstood by unit owners and which often leads to acrimonious arguments in annual general meetings. Often unit owners want more information and more involvement than is appropriate or required by law. Their demands are often accompanied by unwarranted suspicious and aspersions as to the intentions and ambitions of the board. The obvious solution for such unit owners is simple: stand for election to the board yourselves; be volunteers and helpers, rather than thorns in the sides of board members who, typically, are already giving far more time, energy and concern to the welfare of the condominium than the measure of gratitude or support they receive from its owners and residents.

Conscious failure to take reasonable steps to ensure the corporation carries out its objects and performs its duties in accordance with the Act, would violate such standard of care.

### **Conflict of Interest**

In addition to the foregoing comments, acting in “good faith” means that the intentions, as well as the actions, of board members must be focused on the good of the corporation as a whole and not, for example, on such director’s or another unit owner’s personal issues or interests. In conjunction with this, a director must disclose any material direct or indirect interest he or she has in an actual or proposed contract or transaction of the corporation (s. 40(1)).

Subject to limited exceptions, the director having such conflict of interest shall not take part in discussions about nor vote in respect of the contract or transaction, and the director shall not be counted toward quorum in the meeting at which it is discussed (s. 40(6)).

Where a director complies with these requirements and acted in good faith in respect of the contract or transaction in question, the director will not be responsible to report the amount of his or her profit or gain from the contract or transaction, and the contract or transaction is not voidable solely because of the conflict of interest (s. 40(7)). Also, in certain circumstances, even if a director has not fully complied with the disclosure requirements of the Act, the unit owners may approve a contract or transaction in respect of which a director has a conflict of interest (s. 40(8)).

### **Treatment of Corporation Funds**

Unit owners are obligated to pay common expenses, including contributions to the reserve funds of the corporation (s 84(1) and 84(3)).

Whoever receives money paid to the corporation as contributions to the common expenses, including reserve fund contributions, is trustee of the same and must keep and use such funds strictly for the performance by the corporation of its duties and obligations (s. 115(1)).

Improper handling of corporation funds can result in fines to the perpetrators of up to \$100,000 for corporations (i.e., property management companies) and up to \$25,000 for individuals (i.e., directors) (s. 137(1)).

Use of corporation funds for improper purposes is a violation of the Act. Similarly, the failure to use corporation funds for proper and necessary purposes (i.e., for performance of the duties of the corporation) would also violate the Act, in so far as the same would likely involve neglect of the corporation’s obligations.

Each condominium corporation must have at least two bank accounts in its own name: a general account for operating expenses and a reserve fund (s. 115(2)). The operating funds and reserve funds of the corporation must not be co-mingled (s. 115(4)).

Operating funds are used to fulfill the general obligations of the corporation, including regular maintenance costs. The reserve funds of the corporation must be used only for the “*major repair and replacement*” of the common elements and assets of the corporation (s. 93(2) and s. 95(1)).

The board does not require the consent of the unit owners to make expenditures out of the reserve fund of the corporation (s. 95(2)).<sup>4</sup>

The board would require approval from the owners, in the form of a condominium by-law, for any borrowing. This should include a standing by-law that authorizes general borrowing for budgeted expenses (s. 56(1)(d)) and separate by-laws authorizing any specific borrowing that is over and above the expenditures listed in the condominium's budget (s. 58(3)).

There are many other provisions of the Act that detail obligations of the board relating to finances and financial reporting for the corporation. It may be noted there is no specific obligation in the Act to prepare annual budgets for the corporation, but there are many provisions (such as the aforementioned relating to borrowing by-laws) that do not make sense, or cannot be properly complied with, unless the board prepares an annual budget.

### ***Record Keeping and Confidentiality***

There are numerous records of the corporation that the board is required to ensure the corporation maintains (s. 55 and others). In addition, the board is often privy to confidential information of the unit owners and residents and the employees of the corporation.

The corporation is subject of the *Personal Information Protection and Electronic Documents Act* as well as other privacy laws. In addition to complying with other requirements of such legislation, the board must therefore ensure that all personal information collected is stored and treated with significant care and the board must not disclose anything without careful consideration of what is being disclosed, to whom and for what purposes.

Notwithstanding this, in certain circumstances most (but not all) of the records of the corporation are to be accessible to unit owners for examination (s. 55(3)). However, the Act requires that such examination must be for purposes "*reasonably related*" to the purposes of the *Condominium Act, 1998*.

Pursuant to section 55(4), unit owners are not entitled to examine any of the following records:

- (a) records relating to employees of the corporation (other than employment contracts);
- (b) records relating to actual or pending litigation or insurance investigations

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<sup>4</sup> The use of the reserve fund without unit owner approval is consistent with the express duty of the condominium corporation for "repair after damage" of the common elements and assets of the corporation (s. 89(1)). In short, the board has no option, pursuant to its statutory obligations and those of the condominium corporation, to carry out the repairs for which the reserve fund is kept, and therefore does not require further approval for the use of such fund. This is another sometimes "sticky" point for many unit owners. The reserve fund is obviously an important component of their investment in the property, and many owners like to be certain about its use. While there is nothing wrong with this intention, it is nevertheless not a requirement for the board to get unit owner approval for appropriate expenditures from the reserve fund, nor can unit owners' express approval justify any improper use of such funds.

involving the corporation; or

- (c) records relating to specific units and owners (except where the requesting party has a permitted interest in such unit under section 55(5)).

Furthermore, where the corporation has specifically entered into a confidentiality agreement with any party, such agreement should not be breached by disclosure to a unit owner without certainty from legal counsel as to the possible consequences of such disclosure.

A board granting access to records contrary to the provisions of the Act would be in breach of its statutory obligations as well as general legal obligations relating to privacy and confidentiality.

### ***Liability and Indemnification***

Subject to the *Condominium Act, 1998* and the by-laws of the condominium corporation, the board is personally liable for its management of the affairs of the corporation. Failure to comply with the Act, governing documents of the corporation and other applicable law,<sup>5</sup> could result in significant liabilities for the condominium corporation and/or individual directors.

However, pursuant to section 37(3) of the Act, a director shall not be found liable for a breach of his or her duties, if relying in good faith upon:

- (a) the financial statements of the corporation's auditor (or certain other persons), or
- (b) *"the report or opinion of a lawyer, public accountant, engineer, appraiser or other person whose profession lends credibility to the report or opinion"*.

In addition, the corporation must purchase and maintain directors and officers liability insurance if it is reasonably available (s. 39).

Further, the by-laws of a condominium corporation may provide for the indemnification of a director for liabilities arising as a result of carrying out the duties of the board or corporation (s. 38(1)); however, note that pursuant to section 38(2):

*No director or officer of a corporation shall be indemnified by the corporation in respect of any liability, costs, charges or expenses that the person sustains or incurs in or about an action, suit or other proceeding as a result of which the person is adjudged to be in breach of the duty to act honestly and in good faith.*

Michael H. Clifton (April 2008)

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<sup>5</sup> Which includes diligently fulfilling the sometimes uncomfortable duty of requiring the same compliance by unit owners and residents of the condominium.