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Latent Defects and the Law

Buyers Should Beware When Purchasing Older Apartment Building Stock

By Chris Seepe

In December 2014, an Ontario Small Claims Court judge awarded a judgment in favour of a buyer who alleged that the seller had not disclosed a defect that had repeatedly occurred over many years, prior to the selling of the property. The buyer had purchased the three-storey, forty-year-old Durham region apartment building in April 2011. In January 2014, tenants reported substantial deterioration of in-suite walls. Water had entered into the plaster walls and swelled like boils. The buyer also found several areas of uncharacteristic white stains on the external brick walls.

Specialists determined that the cause was condensation forming between the walls, a problem common with buildings built before vapour barriers were mandated in the Building Code. The buyer then learned from a long-term tenant that the wall problems were a regularly recurring event. The tenant swore in an affidavit, which was admitted into evidence in the trial.

The Agreement of Purchase and Sale (APS) included a clause, "The Seller states that, to the best of the Seller's knowledge and belief, there is no known damage to the basement, roof, or elsewhere in or on the property caused by water seepage or flooding."

The Ontario Limitations Act (2002) generally states caveat emptor—"buyer beware." A buyer can only file a claim of defect within two years from the date of purchase, with generally no recourse after that. However, the Act differentiates between two types of defects. A "patent" defect is one that can be discovered

by observation ("obviousness") or inspection using generally accepted industry-standard practices. A "latent" defect is one that is present but is not obvious, visible, apparent or actualized and can't be discovered by industry-standard inspection practices.

A seller has no obligation to disclose a defect that is obvious, such as a clearly-visible water-soaked crack in a foundation wall, and the buyer must be able to prove that the seller knew about a latent defect. If the defect is proved to have existed prior to selling the property but the seller didn't know about it (perhaps the defect didn't appear while the seller owned the property), then the seller can't be held liable.

In the trial referenced above, the tenant's affidavit strengthened the buyer's case. The judge determined that the seller knew, or ought to have known, that there was recurring water damage caused by an untreated defect in the property. The judge stated he "sympathized with the Defendant" but the Defendant clearly breached the "no water damage" clause in the fully-executed APS. SCC can't award punitive damages, and "betterment" costs are excluded—that is, repairs that improved the property. For example, if the original roof was ten years old with a twenty-year life expectancy, the court might rule that the buyer received a betterment of ten years and then award only half the new roof's cost. The buyer was also not permitted to recover their personal expenses related to attending meetings, overseeing repairs, travel etc. Presumably this is because the value of one's time is highly subjective and would inevitably be contested. It could also be a source of considerable abuse in inflating costs.

There are several cases in law regarding the responsibility to disclose material facts: McGrath vs. MacLean (1979), Krawchuck vs. Scherbak (2011), and Dennis v. Gray (2011).

In Krawchuck vs. Scherbak, the real estate agent was found to be 50 per cent at fault for a lack of diligence in reconciling misleading statements made by the client, failing to inform their client of the implications of their false statements, and failing to bring these issues to the attention of the purchaser.

In a decision released in May 2014, a deputy Judge of the Barrie (Ontario) Small Claims Court said in his judgment that a seller must disclose to the buyer anything they know about a defect that has caused any loss of use or enjoyment of a meaningful part of the premises.

Since the case of McLean vs. MacGrath, and in light of Dennis vs. Gray, the principle of caveat emptor appears to be either becoming more specifically defined or more exceptions are occurring. The evolving principle appears to be that if a seller properly discloses an actual or perceived defect in a property, then this should protect them from the risk of litigation and the accusation that the seller didn't comply with their duty to disclose. Perhaps this will mean the seller has to provide a price discount or perhaps it will lead to sellers pricing their properties as they should have been in the first place. Either way, it will still likely be less expensive than settling a court action.

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