Tarion Reform: What it means for Builders

By: Colin Campbell
Introduction

The long awaited Final Report of former associate Chief Justice J. Douglas Cunningham’s independent review of the Tarion Warranty Program has been released to much enthusiasm as well as some quiet concern. Justice Cunningham was appointed by the Provincial Government in 2015 to conduct an independent review of the Tarion Warranty Program (“Tarion”), which administers the Ontario New Home Warranties Plan. The Final Report is the first step in the Government’s response to the growing public scrutiny of Tarion and calls for reform of both the Plan and the Ontario New Home Warranties Plan Act (the “Act”) under which it operates.

The Act gives Tarion the exclusive responsibility of enforcing the warranties provided by new homebuilders, along with regulating those same builders. Measures to reform Tarion have been called for by almost all players in the industry, including homeowners and builders, save and except for Tarion itself, which has grown comfortable with the relative monopoly it now holds. The chief concern is Tarion’s overlapping role in administering the warranty program, regulating builders and vendors, creating the rules regarding warranty protections and adjudicating disputes regarding those rules.

In total, Justice Cunningham has made 37 recommendations to the Government that propose significant changes in how builders and developers will be regulated in the province of Ontario and how new home warranties will continue to be administered and enforced going forward.

The most significant recommendation, and one that the Government has already indicated it will include in new legislation it intends to introduce in the fall, is the creation of an entirely new regulatory body for homebuilders in the Province of Ontario. Further, the Report includes a new model for warranty coverage, changes to the minimum warranty protections, changes to the regulation of builders and vendors, updates to the adjudication of unresolved warranty disputes and increased oversight of warranty standards and coverage.

While the Report proposes many positive and well needed reforms, the spirit of the proposals are focused almost exclusively on homeowners. Any legislation introduced by the government will be sold as strengthening consumer protection measures for owners of newly built homes, unfortunately, at the expense of many hard working and well intentioned builders.

Builders should understand that many aspects of registration or renewal of registration will change, possibly as early as January 1, 2018 and that the requisite requirements may become more difficult for builders to satisfy, while simultaneously, the criteria for determining breaches of warranty will be lowered and it will become easier for homeowners to make claims and have their claims processed. Below is a brief highlight of the more significant proposals contained in the Report.

Recommendations

1. A Proposed New Model of Warranty Coverage

Tarion acts as the sole warranty administrator for new homes, and while the warranty itself is provided by the builder/vendor and not Tarion, Tarion administers the warranty program and enforces the warranty. Tarion does this through the collection of enrolment fees on new homes, by responding to claims where necessary and stepping in to resolve disputes where a homeowner and builder cannot
do so themselves.

The Report acknowledges the unusual nature of this arrangement, noting that in most other jurisdictions across Canada, warranty protection is provided by multiple providers and through a competitive model, similar to that of an insurance product. Tarion however is not subject to any of the same oversight that would ordinarily apply to an insurance company delivering a similar service.

The Report is proposing a new competitive model, which would provide builders (and indirectly homeowners), with a choice of warranty providers. Instead of Tarion being the only administrator of new home warranties, such services would be open to multiple providers, as various agencies and insurance companies have expressed an interest in offering these types of services, and have the necessary expertise to do so, as they do in other provinces. Under this new model, Tarion would continue to operate, under a new name and as a not-for-profit corporation, retaining responsibility for all existing homes currently enrolled with Tarion.

To manage current enrolments (with over 365,000 new homes under warranty protection), Tarion will be transitioned into a new not-for-profit entity that would have nothing to do with regulating builders. The new not-for–profit would then be in a position to compete with other insurance providers and would be subject to the same regulations and oversight. Therefore, builders could choose to continue using the non-for-profit provider or could turn to the private market instead.

The new model would be characterized as an insurance product and therefore would be subject to the provisions of the *Insurance Act* R.S.O. 1990, c. I.8 along with other oversight measures including minimum capital requirements, investment restrictions, reporting requirements and most importantly, a mandatory complaint process, where complaints could be made to the Financial Services Commission of Ontario and the Ombudsman. Each provider would also be required to adhere to minimum standards of warranty protection/coverage that would be determined by the government and clearly set out in the new legislation.

We have long argued that Tarion, while not an insurance company, acts as if it is one, by treating enrollment fees as premiums and arbitrarily paying out claims if and when it feels like it, usually with little or no communication to the builder. In recent years, Tarion has adopted this practice almost exclusively, by paying out settlements to homeowners instead of undertaking to have remedial work done and then invoicing the builder. Tarion generally does this even when the builder is ready, willing and able to perform its warranty obligations but has had its ability to do so thwarted by intransigent homeowners and Tarion’s refusal to assist.

Moreover, Tarion’s settlement payments are often a windfall to homeowners and there are no checks or balances on what monies Tarion pays out, which is almost guaranteed to be well above the actual costs to the builder to remedy warranted items, or is totally disproportional to the actual cost to repair. Ideally, under a new regime, warranty providers will more carefully scrutinize any valid warranted items and the actual cost of repairing those items, before paying out large sums and turning to the builder for indemnity. Any new warranty providers should make efforts to assist builders in fulfilling their warranty obligations and facilitate the actual repairs so homeowners get the remediation they’re entitled to and not a windfall at the builder’s expense.

Whether, this conduct will change under a new model will not be known for some time. Builders, however, can only hope that with multiple providers, greater competition and increased scrutiny,
these providers will be required to deal with builders more fairly, ahead of cutting a builder out of the warranty process entirely and then subrogating against a builder to recover their costs.

Ultimately for builders, these changes mean that Tarion will continue to provide warranty services under the new model, and much in the same way, at least until new providers can catch up. Regardless of the provider, the warranties provided by the builder will be similar if not the same as the current 1st, 2nd and 7 year warranties provided now. Ideally, once builders start to utilize other providers, Tarion’s role will become increasingly marginalized and it may have to begin treating builders fairly to compete for their business, as the builders choose which provider to use.

2. Changes to the Regulation of Builders and Vendors

Along with Tarion losing its monopoly on providing warranty protection, Justice Cunningham has proposed that Tarion be stripped of its role as the regulator of new homebuilders.

This is in direct response to the perceived or real conflict of interest created by Tarion being both the regulator of builders and the provider of warranty protection, while also being the body with sole discretion to create the rules under which it operates, and adjudicate disputes initially.

Going forward, the Province would assume responsibility for regulating homebuilders which is more consistent with other delegated administrative authorities, such as the real estate sector, which does not have the power to set its own regulations. Bringing the regulatory role of Tarion under government control, with the creation of a new stand-alone agency or administrative authority, closely connected to the Government, will allow for increased transparency and greater oversight of the regulatory function. Presently Tarion is not subject to any mandatory Government oversight, let alone the Auditor General or Ombudsman. The new body would have annual reporting requirements and be subject to ministerial audits and other financial reviews.

The Report also proposes changes in the way builder eligibility for registration would be determined. It recommends that any new Act clearly set out the core elements of eligibility and have a more clearly defined framework for determining eligibility. At present, Tarion assesses all aspects of a builder’s current and past history without any defined limits, often making its decisions arbitrarily to justify a refusal of an application or renewal.

While Justice Cunningham proposes that the eligibility requirements be better outlined, he also recommends that the regulator more carefully scrutinize builders who seek registration. The Report speaks about extending the review of a builder’s prior history or past conduct to include other individuals who may play or have an active or key role in a builder’s business, including shareholders, employees, agents and subcontractors.

The Government’s new regulatory agency would also be equipped with greater compliance and enforcement tools, including the ability to level “administration penalties”, such as fines, against a builder as an alternative to prosecution or revocation of registration. In addition, it is recommended that the regulator have the ability to issue compliance orders where a builder has failed to comply with the legislation, the ability to seek the appointment of a court appointed receiver where there is evidence of financial problems or the ability to apply for a court order to freeze assets. These recommendations seem somewhat draconian to the average sized builder, who makes up 80% to 90% of all builders.
Perhaps the most concerning of Justice Cunningham’s proposals seeks to give the new regulator the authority to suspend a builder’s registration immediately without the need to issue a notice of proposal thereby denying the builder any procedural fairness or an ability to defend such a proposal. Such action would also have serious consequences on the construction of larger projects in active development, where multiple trades are on site and money is flowing through the construction pyramid.

The Report also expands on the current technical competency and education requirements of builders to suggest that where a builder relies on other individuals to complete and oversee the construction of a new home, those individuals, in addition to the builder, should be required to meet the minimum technical competencies. Therefore in instances where a corporate entity or a partnership is seeking registration status, it may be the case that multiple individuals must complete written examinations and interviews and not just the individual builder.

In addition, the Report also recommends expanding on Tarion’s builder directory which allows the public to view information about a registered builder, including whether there have been any chargeable conciliations made and the number of possessions in a year. The Report proposes that the public directory go further to include more information about the history of a builder such as other discipline proceedings, provincial offences and more detailed claims data, showing exactly what claims have been settled by Tarion (whether they are for defects related to a 1st, 2nd or MSD claim), as well as showing information of deposit and delayed occupancy claims.

3. Changes to the Dispute Resolution Process

Disappointingly, the Report does little to address problems for builders regarding the dispute resolution process, but includes changes that will make it easier for homeowners to make warranty claims and to access the dispute resolution process to their benefit. This is especially surprising considering that Justice Cunningham’s Interim Report included some indication that builder’s remedies, such as the Builder Arbitration Forum (“BAF”) should be addressed and improved. While this article is not about the BAF, we have written previously on how builders are disadvantaged when appealing disputes with Tarion on warranty claims.

Justice Cunningham does acknowledge that the current conciliation process under Tarion means different things to different stakeholders; where homeowners may view Tarion as their friend or as more supportive of the builder, builders often feel pressure to repair items that are not properly warranted or that Tarion is simply motivated to pay settlements to appease an insistent or bothersome homeowner.

Whichever narrative one subscribes to, the common theme is that Tarion has simply become too arrogant for its own good. When Tarion makes a decision there is almost no room for a builder or a homeowner to dispute such a decision without having to undertake a costly appeal. Tarion knows this and uses it to its advantage. Where Tarion spends millions of dollars each year in arbitrations or lawsuits, with money taken from builders in the form of registration fees, homeowners and builders must personally fund their appeals in instances where they feel strongly enough about the wrongness of a Tarion decision. The consequence is that it is almost always too costly for a homeowner or a smaller builder to dispute warranty decisions as they simply do not have the same resources as Tarion.
Be that as it may, it appears as if little will change apart from the fact that the homeowners will be required to deal with the warranty provider chosen by their builder. Homeowners will continue to have access, as they do now, to an independent adjudicator where they challenge a decision made by the warranty provider.

The role of the warranty provider will also remain largely the same, and the conciliation process proposed is almost identical to the one already in place under Tarion. Under the new regime, homeowners may still make initial complaints about deficient items, a builder will have an opportunity to inspect and repair those complaints. The warranty provider may then, upon request, review the claim and conduct an assessment of warrantability. Where the parties cannot resolve the complaints, the warranty provider, will step into the role of an adjuster, assess the claims and arrange for work to be done.

The Report recommends no substantive changes to the funding of the proposed conciliation process, and the relatively minor administrative costs of requesting conciliation will still be born up front by the homeowners. The Report does suggest that in some cases it may be appropriate for a condominium corporation to bear the costs of the adjudicative hearings as they are perceived to be in a better position financially to absorb the costs.

**A Lower Standard - Onus of Proof**

Of significance to builders are recommendations that any new legislation clarify the ambiguity that exists with respect to the onus of proof in relation to warranty claim. The Report takes the position that homeowners are at a severe disadvantage when making warranty claims as they are usually not experts in the field of construction, when compared to their builder. Therefore, under the new regime, homeowners would only be required to provide the necessary supporting documents setting out a description of symptoms and will not be expected to prove the cause of a deficiency.

While it would be helpful to articulate a set standard of proof, it is not our experience that homeowners are disadvantaged as compared to builders. Currently, all a homeowner is required to do is submit a warranty claim within the prescribed period and wait for Tarion to get involved. Often, the homeowner then refuses a builder’s proposed method of repair or denies the builder access to inspect items or make repairs, with the intention of having Tarion step in and cash settle the warranty claim directly.

Proposals to lower the threshold will likely lead to more warranty claims by homeowners and more work for builders in responding to those claims that are without merit.

As is our experience, some homeowners see Tarion as a free cheque and therefore attempt to have as many items as possible found warranted by Tarion. Changes need to be designed to assist homeowners with genuine problems and not reward behaviour that attempts to claim as many items as possible in the hope of a payout rather than allowing a builder to fulfil its warranty obligations.

4. **Other Matters**

**Illegal Building**

The Report only briefly touches on the ongoing problem of illegal building in Ontario and the “owner-
“owner-built” exception to the mandatory enrollment of new homes. Currently, where a home is being built for personal occupancy, there is no requirement to enroll the home with Tarion for warranty protection. While warranty coverage is available for all new homes, even where the home has not been enrolled, coverage is not available for those who qualify for the “owner-built” exception. This captures the situation where an individual builds a home for his or herself and not for resale or to flip for a profit.

Problems have arisen in circumstances where an owner’s intentions change or where builders are abusing this exemption for the purpose of regularly building and selling homes without warranty coverage. The Report points to a relatively new pilot program instituted by Tarion and running in several municipalities across Ontario (not Toronto) in which the municipality requires a “Letter of Confirmation” from Tarion, where the builder/vendor is taking out a building permit and purports to qualify for the owner-occupied exception. In this case, the builder must first satisfy Tarion that the owner builder exemption applies and that enrolment of the home is not required, before a building permit is issued and before construction begins.

The Report proposes that the new legislation go even further and calls for a system of mandatory enrollment and mandatory warranty coverage for all new homes, including those built for personal occupation. Mandatory enrolment would force all new homes to have warranty coverage even if owner built and would effectively solve the ambiguity around the owner build exception by eliminating it. However, it would force the person proposing to build their own home to register as a builder.

**Definition of “Home”**

Related to the issue of illegal building, the Act currently excludes previously occupied homes from warranty coverage but does not define what previously occupied actually means. There is no set formula to determine whether a new home has been previously occupied and therefore ineligible for warranty coverage. Justice Cunningham proposes that any new legislation clearly define what degree of previous occupation results in no warranty protection under the definition of “previously occupied”. This would provide certainty to the owner occupied exception and go a long way to solving problems of illegal building but so would the mandatory enrollment of all new builds as proposed above.

**Deposit Protection**

The Report is recommending an immediate review of the limits of deposit protection. Presently the Act provided a warranty on deposits up to a maximum up to $40,000 for freehold homes and $20,000 for condominiums. The Report recommends that these amounts should not be fixed and instead be indexed or tied to the actual price of the home. Builders should expect some allowance for these limits to increase.

The Report also addresses the fact that only condominium deposits require the builder to hold said deposits “in trust” in accordance with the Condominium Act 1998, S.O. 1998, c. 19; therefore in the event of a builder failure, (absent fraud or criminal behaviour), deposits are available to reimburse new home purchasers. It is proposed that the trust obligation be extended to freehold townhomes without negatively affecting smaller builders. In addition, there would be no distinction between monies paid toward the purchase price and amounts paid for upgrades under an agreement of purchase and sale, with all monies paid in advance, treated as deposit monies that will benefit from deposit protection.
Conclusion

While the Report has proposed much needed reform, it has also come up short on acknowledging difficulties experienced by small to medium sized builders, who like homeowners, have experienced their share of frustration with Tarion.

This is not surprising, as it is much easier for the Government to sell any new legislation as a consumer protection measure rather than an effort to assist builders and developers. This, however, is unfortunate, given the climate of soaring housing prices and a severe shortage of new and affordable freehold homes. The Government should not miss this opportunity to consider measures to help encourage new home building instead of discouraging it.

Ultimately, the report is substantial but provides only a glimpse into what the Government’s proposed legislation will look like. What is certain is that Tarion will lose its role as the regulator of new home builders and will only continue to operate in a relegated capacity, as a not-for-profit warranty provider, competing with other insurance companies offering the same service.

While it is too early to tell how the proposed legislation will truly affect homeowners and builders, based on the proposals made by Justice Cunningham, it is clear that wholesale change is coming and that such change is welcome, perhaps not by Tarion but by both homeowners and to a lesser extent, builders. The most important thing the Government can do is to bring some much needed accountability to the bodies charged with regulating builders and providing warranty coverage. If Tarion is good at one thing, it would be congratulating itself on just how well it does its job; the trouble for Tarion is, there is no longer anyone listening.

This material does not constitute legal advice. Readers are urged to consult their professional advisers prior to acting on the basis of material in this publication.