Focus REAL PROPERTY

Looking too hard can undo indoor management rule

Ray Mikkola

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You have been retained to act on a mortgage transaction. The lender (or its counsel) requires you to opine as to the due execution and delivery of the loan documents, and that the borrower, your Ontario Business Corporations Act (OBCA) or Canada Business Corporations Act (CBCA) corporate client, is well and truly bound by the loan documents, including the mortgage. (There will typically follow the elaborate dance between counsel as to the need for an "enforceability opinion," but don't get me started on that.)

In order to provide the due execution opinion, it seems to me that real estate lawyers currently employ a wide variety of due diligence. Some rely entirely on an officer's certificate and limit their opinion accordingly. Others undertake a detailed review of the corporate minute book (taking that opportunity to cooper up any missing signatures or other corporate deficiencies), while others issue the opinion and expect that title insurance will surely protect the lender from any claim arising from the lender's reliance on what appear to be properly executed documents.

I expect that all of us will at least confirm the existence of the corporation and review the publicly available record of directors as a requirement to issue any opinion. But in view of the indoor management rule, codified (and enhanced) by section 19 of the OBCA (section 18 of the CBCA), I wonder why as borrower's counsel we do anything more. In the absence of knowledge to the contrary, it seems to me that the lender is as entitled to rely on the rule as we are as solicitors, with respect to the due execution of the documents.

Broadly speaking, the common law version of the indoor management rule was set out in a 1915 decision of the Supreme Court of Canada. The court held that persons are required to read the statute under which a corporation was incorporated and to review any publicly available documents to confirm that the proposed dealings by the corporation are not inconsistent therewith, but that there is no need to inquire as to the "regularity of internal proceedings" because the person could rely on the assumption that all was being done in the usual course (*J.H. McKnight Construction Co. v. Vansickler* [1915] S.C.J. No. 22). The OBCA and CBCA rule goes further by prohibiting inter alia the corporation from raising as a defence non-compliance with anything contained within the articles. Not surprisingly, reliance on the rule is qualified where "the person has or ought to have, by virtue of the person's position with or relationship to the corporation" knowledge of any of the numerous matters that might otherwise be raised by the corporation as a defence. But it seems to me that constructive knowledge of, for example, restrictions or prohibitions in the articles of a corporation by reason of their being available on a public register (which the person dealing with the corporation could have reviewed) has been ousted by the express provision in section 19 of the OBCA that a corporation may not raise non-compliance with its articles as a defence in any claim by such person.

The rule may not apply to non-OBCA/CBCA corporations, though. For example, the Alberta Court of Appeal in *Condominium Plan No. 8222909 v. Francis* [2003] A.J. No. 976 held that the rule does not apply to a condominium corporation. Neither the Alberta *Condominium Property Act* nor the Ontario *Condominium Act* contain a statutory equivalent to section 18 or 19 of the CBCA and OBCA, respectively.

In my view, the broad wording of the OBCA and CBCA rule expressly excuses the requirement to review the minute book, articles or any corporate documents listed in these acts in the course of giving due execution and authority opinions in standard real estate mortgage transactions involving business corporations where the lender is acting at arm's length to the corporation. Indeed, it seems to me that such person will be entitled to the protection of the OBCA and CBCA where the lawyer merely confirms that the person executing the mortgage is the person indicated as a director in the most recent public filing, and that the corporate borrower is a valid and subsisting corporation, and without the requirement to provide any opinion. Any further and additional due diligence might serve to undo the third party's entitlement to rely on the rule. Relying only on the rule would achieve cost savings, enhance business practicalities and allow such parties the full benefit of the codified and enhanced rule.

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Lawddities

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Red hot Ferrari lands rich kid in court

Many young men like to buy new cars, but the son of a Swiss multimillionaire cut some legal corners in order to realize his dream. The 20-year old became bored with his old model Ferrari 458 Italia, reports the U.K.'s Daily Mail. However, the over $300,000 car was appraised at much lower than the latest model. The solution was to set it on fire and collect the insurance. Accordingly, the man drove the car to a car park in Augsburg, Germany, and hired two accomplices for about $20,000 to immolate it while he went to a local massage parlour. Security camera footage and phone recordings documented the crime and the three were convicted. After learning that the young man received a large monthly stipend from his father and owns 15 other cars including a Lamborghini, an Augsburg judge sentenced him to 22 months' probation and a fine of 30,000 euros. The accomplices received probations between 14 and 16 months. His explanation in court was that he was low on cash but afraid to tell his father that he was bored with the Ferrari. – **STAFF**