

Defence & Indemnity

February 29, 2016

V. SURETY AND BOND ISSUES

The relationship between trust and lien claims under Provincial builders' lien legislation

***Stuart Olson Dominion Construction Ltd. v. Structal Heavy Steel, 2015 SCC 43*, per Rothstein, J.**

I. FACTS AND ISSUES

Stuart Olson Dominion Construction Ltd. ("Dominion") was the general contractor of a football stadium in Manitoba (the "Project"). The owner of the Project was BBB Stadium Inc. (the "Owner"). Dominion entered into a subcontract with Structal Heavy Steel ("Structal") to supply and install structural steel work for the Project.

Dominion began withholding payments to Structal and stated it was setting off against the unpaid amounts for back charges it claimed resulted from delays attributable to Structal. In September 2012, Structal filed a builder's lien against the Project Lands for approximately \$15 Million, consisting of unpaid progress payments, unpaid statutory holdback, and a large delay claim of its own. The lien resulted in the Owner not making further payments to Dominion.

In October 2012, Dominion paid into Court a lien bond in the full amount of the lien. This bond provided that if Dominion did not satisfy any lien judgment against it, the surety of the lien bond would pay, up to an express maximum, the amount of the lien judgment. Structal approved the bond and vacated its lien, which Dominion expected would result in the Owner releasing to Dominion the progress payments being held back by the Owner as a result of the lien.

Structal continued to demand payment from Dominion, asserting that Dominion was required to comply with the trust provisions of the Manitoba's *Builders' Lien Act*, CCSM c. B-91 (the "MBLA") and was not entitled to any set off against the funds held in trust. The trust provisions in the MBLA impressed any funds received by Dominion from the Owner with a trust for the benefit of Dominion's subcontractors (one of whom was Structal) and expressly prevented Dominion from appropriating or converting the received funds for its own use until all of its subcontractors had been paid.

In addition to demanding payment from Dominion, Structal also put the Owner on notice that if it paid the funds (currently being held back by the Owner) to Dominion, the Owner would expose itself to a breach of trust claim to be made against it by Structal. Under the MBLA, an owner is also subject to its own express trust obligations. This notice by Structal resulted in the Owner not making any further payments to Dominion, despite the discharge of Structal's lien.

Dominion refused to make any payments to Structal, arguing that Structal was fully secured by the lien bond, that there was no breach of trust, and that Dominion had a set-off against the monies claimed by Structal.

Dominion applied to the Manitoba Court of Queen's Bench for a declaration that it had satisfied its *MBLA* trust obligations to Structal, which declaration would then allow it to receive payment from the Owner. In response, Structal filed a motion requiring full payment of its past-due invoices, without deduction or set-off, upon Dominion receiving the funds from the owner.

Dominion's position was that it should not have to pay amounts twice, once into Court (in the form of the lien bond, for which it was paying a premium to its surety) for the removal of the lien, and then again to secure its trust obligations.

The Manitoba Court of Queen's Bench held that the filing of the lien bond extinguished the trust obligations of Dominion pursuant to *MBLA* and stated that Dominion could do as it wished with the funds once received from the Owner. The Court of Appeal overturned this decision and concluded that under the *MBLA*, subcontractors have two separate and distinct rights beyond the common law right to sue for breach of contract: the right to the statutory trust and the right to file a lien claim against the property.

II. HELD: Appeal dismissed: the filing of the lien bond did not extinguish the statutory trust conditions

1. The Supreme Court of Canada upheld the decision of the Manitoba Court of Appeal and affirmed that the *MBLA* provides two separate, legislative remedies to those who provide services or materials to a construction project: construction liens (section 13) and statutory trusts (sections 4 and 9). A contractor or subcontractor can have both a lien claim and a trust claim and these different remedies serve different purposes.

(a) The purpose of a lien is to "creat[e] charges against the land in favour of those contractors, suppliers and workers who can prove their claims" (at para. 19 citing ***Provincial Drywall Supply Ltd. v. Gateway Construction Co.*** (1993), 85 Man. R. (2d) 116 (MBCA) at para 47). Liens create considerable impediments to liquidity since a lien creates an encumbrance on the land. To address the barrier created by a lien claim, the *MBLA* provides for vacating the lien if alternative security is posted, pending resolution of the validity of the lien claim. Accordingly, the *MBLA* provides that the land can be freed from the lien encumbrance while simultaneously protecting the lien claim.

(b) Alternatively, the purpose of the statutory trust is "to help assure that money payable by owners, contractors and subcontractors flows in a manner which is in accord with the contractual rights of those engaged in a building project and that it is not diverted out of the proper pipeline" (at para 40 citing ***Provincial Drywall Supply Ltd. v. Gateway Construction Co.***, supra at para 47).

(c) Trust claims are not extinguished by filing of a lien bond, as a lien bond only provides security for a lien claim. If a lien is invalid, any claim against a lien bond is extinguished and the lien claimant would then be unable to access to the funds guaranteed by the bond. However, a contractor or subcontractor may still have a trust claim. The existence of the trust remedy is unaffected by the filing of a lien bond, which is consistent with the *MBLA*'s provision that the contractor is barred from diverting trust funds for its own use until all subcontractors have been paid.

2. Dominion argued that there was a risk of double compensation where the lien and trust claims were for the same work, services, or materials. In response, the Supreme Court articulated the distinction between payment and security:

To the extent that the lien and trust claims are for the same work, services, or materials, payment under the trust will eliminate the equivalent amount payable to satisfy the lien claim. In the present case, Structal acknowledges that, had Dominion paid the trust monies into court, there could have been a reduction in the amount of the lien bond by an amount equivalent to the monies paid into court. Dominion chose to provide security by way of a lien bond rather than payment of funds into court. [...] It is true that [Dominion] paid premiums for that bond which are not recoverable, but that is simply the cost of the security which it chose to provide. Structal will not receive double payment. (at para 48-49)

3. The Supreme Court also explained that had Dominion decided to pay cash into Court instead of a lien bond, it would have avoided the problem of having to "pay twice", once to vacate the lien and once to secure its trust obligations, as a payment of the trust funds into Court would have provided security for the lien and complied with the trust obligations in the *MBLA*:

There may be circumstances where a contractor will choose to maintain double security where there are lien and trust claims for the same work, services, or materials, by acquiring a lien bond while still holding trust funds. However, a contractor can avoid double security by paying cash into court pursuant to s. 55(2) instead of depositing a lien bond. The *BLA* provides that any owner, contractor, or subcontractor with trust obligations "shall not appropriate or convert any part of the trust fund to or for his own use or to or for any use not authorized by the trust" until one of the listed steps has occurred (ss. 4(3), 4(4) and 5(3)). Payment of the trust funds into court to vacate a lien, for the amount of the lien claim implicated by the trust claim, does not constitute an appropriation or conversion of the trust funds. The contractor is doing exactly what the *Act* requires — ensuring the monies are held in trust for the beneficiary. These funds remain impressed with the trust; should

the lien claim fail while the trust claim is outstanding, the cash would continue to be trust funds when returned to the owner, contractor, or subcontractor. So long as the trust funds themselves are deposited with the court, the funds are secure and the trust has not been breached. (at para 46).

III. COMMENTARY

This decision is a reminder of the existence of trust claims under provincial builders' lien legislation and confirms that such trust claims are independent of one's lien rights and remedies. Lien rights and remedies are subject to strict timing requirements. A lien claimant must be sure it complies with these timing requirements or it loses its lien rights and remedies. Trust claims are not subject to any such strict timing requirements and could be advanced well after subcontractor has completed its work and left the project site.

It is critical to note that this case arose from a dispute governed by the Manitoba *Builders' Lien Act*. Provincial lien legislation varies between the provinces in many important ways. There are some important differences between the Manitoba *Builders' Lien Act* and the Alberta *Builders' Lien Act*. For example, the trust provisions in the Alberta *Builders' Lien Act* are much weaker:

1. An Alberta owner is never subject to any trust obligations (Structal could not have convinced an Alberta owner that it would be exposed to a breach of trust claim by releasing funds to its contractor);
2. No trust obligations arise unless a certificate of substantial performance is issued (If no certificate of substantial performance issued, then there are no trust obligations);
3. Only payments received after the certificate of substantial performance is issued are held in trust (typically this would only be the hold back and value of work completed after the issuance of a certificate of substantial performance);
4. There is no express language stating what can or cannot be done with trust funds, only that funds are held in trust (thus there is uncertainty as to the extent of the trust obligations);
5. The restrictions on the use of trust funds does not prevent a contractor or subcontractor from paying other subcontractors or suppliers on a project to whom money is owed; and
6. There are no penalty provisions for a breach of trust, whereas in the Manitoba *Builders' Lien Act* a breach of trust is a summary offence which a penalty of a fine up to \$50,000 or imprisonment up to two years.

A trust claim in Alberta does not result in an encumbrance to land and does not prevent the flow of contract funds as a lien does. While a claimant may have both a trust claim and a lien claim, it is the lien claim which will continue to take on the most importance in the eyes of those higher up the contractual chain, as the registration of a lien prevents an owner from making any further payments (s. 18).

the certificate of substantial performance is issued will be subject to trust obligations. While those obligations prevent it from spending or using that money for other purposes, these funds do not have to be paid anywhere specific, can be used to pay other subcontractors or suppliers on the project or can be held pending the resolution of a claimant's lien and trust claim subject to any claims for set-off that may exist. Practically, as long as a contractor receiving trust funds can make a subcontractor with a trust claim whole, there is unlikely to be any loss to that subcontractor.

It will be interesting to see the extent that this decision results in more payments of cash into Court versus posting of lien bonds into Court in Alberta. Payments of cash into Court as security have their own disadvantages as they are potentially subject to claims of other parties like the Canada Revenue Agency like occurred in ***Japan Canada Oil Sands Ltd. v. Stoney Mountain Steel Corp.***, 2001 Carswell Alta 732, 93 Alta. L.R. (3d) 54, 290 A.R. 251.

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YELLOWKNIFE

601 - 4920 52 ST
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867-920-4542

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