

December 19, 2001

Peter Grimes
Counsel
Department of Public Works
and Government Services
Place du Portage, Phase III, 1C2
11 Laurier Street
Hull, QC K1A 0S5

Dear Mr. Grimes,

Re: Proposal for Federal Construction Trust Legislation

Further to our discussion at the October 12, 2001 meeting between the Canadian Bar Association and the Department of Justice, I am writing on behalf of the CBA's National Construction Law Section (the Section) to urge the federal government to adopt construction trust legislation for federal Crown construction projects. Details of our proposal are set out below.

Proposal

The Section proposes federal legislation, as set out in Schedule A, which reflects sections 8, 10-13, and the relevant portions of s. 39 of Ontario's *Construction Lien Act*.¹ We have used the Ontario *Act* because it is often used as a template in other jurisdictions. Also, courts interpreting any federal legislation could rely on a significant body of well-reasoned case law which has developed over the past 20 years under the Ontario *Act*. The Ontario legislation was recently updated after thorough government study. It also applies to provincial Crown projects.

Our primary purpose is to maintain the *status quo* for the federal Crown while providing a remedy to assist those below the general contractor in the construction pyramid in collecting money owed on federal Crown projects. Our proposal would eliminate owner's trust provisions to avoid any Crown involvement in either the administration or application of the proposed legislation. For that reason, we have omitted a provision similar to section 39 of the Ontario *Construction Lien Act*.

¹ R.S.O. 1990, c. 30. For convenience, we have reproduced the relevant provisions of the Ontario legislation and indicated the changes that should be made.

The Section's proposal would clarify that contractors cannot assign the proceeds of a Crown construction contract. Instead, they would be required to allow the proceeds to flow down to the trades and workers who actually worked on the Crown project.

The federal government has jurisdiction over "the Public Debt and Property".² This makes it constitutionally competent to enact laws concerning property owned by the federal Crown, including improvements to federal Crown lands. In Ontario, there is authority for the proposition that the trust provisions of the *Construction Lien Act* do not apply to federal Crown projects.³

Need for Legislation

The federal government has attempted to protect trades who are working on federal Crown projects by using tender provisions and general contract provisions requiring money to flow down the construction pyramid. While these non-legislative steps are significant, unfortunately they do not provide sufficient protection.

In our experience, the present system does not ensure that trades lower down in the construction pyramid get paid for their work. Instead of paying sub-trades, contractors often use money from federal Crown projects to pay their personally guaranteed debt or to pay more urgent debts not associated with the project. Because provincial legislation prohibits this behaviour on private job sites, contractors frequently siphon money from federal Crown projects to pay debts in respect of work on private job sites to avoid personal liability.

These practices are unacceptable. Aside from increasing the risk of non-payment, they often result in work slowdowns while trades wait for payment. They also require contractors to submit higher bids on federal projects to reflect the credit risk associated with non-payment. This increases the cost of federal Crown construction projects, in terms of both initial bid prices and delayed completion dates resulting from work slowdowns.

The use of tender provisions and general contract provisions is fundamentally flawed because of the doctrine of privity of contract. Sub-trades aren't parties to the obligations between the contractor and the federal government, so they aren't entitled to sue when there is a breach of these obligations. While equitable and other doctrines might assist unpaid sub-trades, their uncertain application would likely lead more to litigation than compensation. The Ontario legislation, upon which our proposal is based, is clear and easily applied. It has a proven track record as a self-help remedy for unpaid trades. These trades can add the trust remedy to pre-existing lawsuits for unpaid invoices on federal Crown projects.

² *Constitution Act, 1867*, s. 91(1A).

³ D.W. Glaholt, *Construction Trusts* (Toronto: Carswell, 1998) at 72.

Benefits

Our proposal would have a number of benefits. These include:

- The government would not be exposed to legal liability resulting from a breach of trust or other claim. The funds paid by the Crown to the contractor would only be impressed with a trust once they were in the contractor's hands. Sub-contractors could not, therefore, claim directly against the Crown for breach of trust, as only the contractor would be a trustee of the funds;
- The proposal would be a self-help remedy which would not cost the federal government anything to administer. Trades would simply sue their contractor in the superior court of a province or territory, adding the trust claim to their claim for simple breach of contract. The government would not be involved in any lawsuit and would not have any responsibilities under the proposal.
- The proposal would actually reduce the government's costs, in terms of both lower bid amounts (recognizing the reduced credit risk of non-payment) and fewer construction delays (with fewer work slowdowns during periods of trade non-payment).
- In a bankruptcy of the general contractor, the statutory trust would preserve construction trades' prior claims. This would reduce the government's cost of replacing the bankrupt contractor where the bankrupt contractor has not paid the existing trades;
- The present system works best when the Department of Public Works and Government Services can hold back money from the general contractor or threaten termination of the general contract. The remedy we have proposed addresses the situation where money has already left the government's hands and the project has been substantially completed. As such, government would not be required to change its contract terms, including holdback provisions and bonding requirements;
- The remedy would not increase litigation because trades would sue on their unpaid debt in any event. Our proposal would increase the trades' chances of recovering the judgment debt, given that a trust would survive a bankruptcy and would impose personal liability on a contractor's directors and officers;
- The proposal helps to ensure that trades actually get paid for the work they do; and
- Using a trust to funnel money from the Crown to trades and labourers who actually do the work is consistent with the general prohibition on the assignment of Crown debts found in s. 67 of the *Financial Administration Act*, R.S.C. 1985, c. F-11.

Conclusion

We appreciate the opportunity to provide you with our proposal. This important initiative would ensure fairness for trades working on federal Crown projects, while at the same time eliminating any risk of liability or cost of administration to the federal government.

If you have any questions or concerns, please do not hesitate to contact us through Richard Ellis, Legal Policy Analyst at the CBA's National Office (tel: (613)237-2925, ext 144; email: richarde@cba.org).

Yours truly,

Jane Sidnell
Chair, National Construction
Law Section

c.c. David Debenham, Stanley Naftolin, Q.C., Co-Chairs, National Construction Law Section
Working Group on Construction Trusts
Canadian Construction Association
Canadian Construction Association, General Contractors Council
Canadian Construction Association, Trade Contractors Council
Surety Association of Canada

SCHEDULE A: THE PROPOSAL

“contract” means the contract between the owner and the contractor, and includes any amendment to that contract;

“contractor” means a person contracting with or employed directly by the owner or an agent of the owner to supply services or materials to an improvement;

“improvement” means,

- (a) any alteration, addition or repair to, or
- (b) any construction, erection or installation on,

any land, and includes the demolition or removal of any building, structure or works or this Act thereof, and “improved” has a corresponding meaning;

“interest in the premises” means an estate or interest of any nature, and includes a statutory right given or reserved to the Crown to enter any lands or premises belonging to any person or public authority for the purpose of doing any work, construction, repair or maintenance in, upon, through, over or under any lands or premises;

“land” includes any building, structure or works affixed to the land, or an appurtenance to any of them, but does not include the improvement;

“materials” means every kind of movable property,

- (a) that becomes, or is intended to become, part of the improvement, or that is used directly in the making of the improvement, or that is used to facilitate directly the making of the improvement,
- (b) that is equipment rented without an operator for use in the making of the improvement;

“owner” means any person, including the Crown, having an interest in a premises at whose request and,

- (a) upon whose credit, or
- (b) on whose behalf, or

(c) with whose privity or consent, or

(d) for whose direct benefit,

an improvement is made to the premises ~~but does not include a home buyer;~~

“price” means the contract or subcontract price,

(a) agreed upon between the parties, or

(b) where no specific price has been agreed upon between them, the actual value of the services or materials that have been supplied to the improvement under the contract or subcontract;

“services or materials” includes both services and materials;

“subcontract” means any agreement between the contractor and a subcontractor, or between two or more subcontractors, relating to the supply of services or materials to the improvement and includes any amendment to that agreement;

“subcontractor” means a person not contracting with or employed directly by the owner or an agent of the owner but who supplies services or materials to the improvement under an agreement with the contractor or under the contractor with another subcontractor;

“supply of services” means any work done or service performed upon or in respect of an improvement, and includes,

(a) the rental of equipment with an operator, and

(b) where the making of the planned improvement is not commenced, the supply of a design, plan, drawing or specification that in itself enhances the value of the owner's interest in the land,

and a corresponding expression has a corresponding meaning;

When materials supplied

_____(2) For the purposes of this Act, materials are supplied to an improvement when they are,

- (a) placed on the land on which the improvement is being made;
- (b) placed upon land designated by the owner or an agent of the owner that is in the immediate vicinity of the premises, but placing materials on the land so designated does not, of itself, make that land subject to a lien; or
- (c) in any event, incorporated into or used in making or facilitating directly the making of the improvement.

*Contractor's and subcontractor's trust,
amounts received a trust*

8.--(1) All amounts,

- (a) owing to a contractor or subcontractor, whether or not due or payable; or
- (b) received by a contractor or subcontractor,

on account of the contract or subcontract price of an improvement constitute a trust fund for the benefit of the subcontractors and other persons who have supplied services or materials to the improvement who are owed amounts by the contractor or subcontractor.

Obligations as trustee

_____(2) The contractor or subcontractor is the trustee of the trust fund created by subsection (1) and the contractor or subcontractor shall not appropriate or convert any part of the fund to the contractor's or subcontractor's own use or to any use inconsistent with the trust until all subcontractors and other persons who supply services or materials to the improvement are paid all amounts related to the improvement owed to them by the contractor or subcontractor.

Vendor's trust, amounts received a trust

~~_____9.--(1) Where the owner's interest in a premises is sold by the owner, an amount equal to,~~

- ~~(a) the value of the consideration received by the owner as a result of the sale,~~

~~less,~~

- (b) ~~the reasonable expenses arising from the sale and the amount, if any, paid by the vendor to discharge any existing mortgage indebtedness on the premises;~~

~~constitutes a trust fund for the benefit of the contractor.~~

Obligations as trustee

~~_____ (2) The former owner is the trustee of the trust created by subsection (1), and shall not appropriate or convert any part of the trust property to the former owner's own use or to any use inconsistent with the trust until the contractor is paid all amounts owed to the contractor that relate to the improvement. R.S.O. 1990, c. C.30, s. 9.~~

Payment discharging trust

_____ 10. Subject to Part IV (holdbacks), every payment by a trustee to a person the trustee is liable to pay for services or materials supplied to the improvement discharges the trust of the trustee making the payment and the trustee's obligations and liability as trustee to all beneficiaries of the trust to the extent of the payment made by the trustee.

Where trust funds may be reduced

_____ 11.--(1) ~~Subject to Part IV~~, a trustee who pays in whole or in part for the supply of services or materials to an improvement out of money that is not subject to a trust under this Act may retain from trust funds an amount equal to that paid by the trustee without being in breach of the trust.

Application of trust funds to discharge loan

_____ (2) ~~Subject to Part IV~~, where a trustee pays in whole or in part for the supply of services or materials to an improvement out of money that is loaned to the trustee, trust funds may be applied to discharge the loan to the extent that the lender's money was so used by the trustee, and the __ application of trust money does not constitute a breach of the trust.

Set-off by trustee

_____ 12. ~~Subject to Part IV~~, a trustee may, without being in breach of trust, retain from trust funds an amount that, as between the trustee and the person the trustee is liable to pay under a contract or subcontract related to the improvement, is equal to the balance in the trustee's favour of all outstanding debts, claims or damages, whether or not related to the improvement.

Liability for breach of trust by corporation

_____ 13.--(1) In addition to the persons who are otherwise liable in an action for breach of trust under this Act,

- (a) every director or officer of a corporation; and
- (b) any person, including an employee or agent of the corporation, who has effective control of a corporation or its relevant activities,

who assents to, or acquiesces in, conduct that he or she knows or reasonably ought to know amounts to breach of trust by the corporation is liable for the breach of trust.

Effective control of corporation

_____(2) The question of whether a person has effective control of a corporation or its relevant activities is one of fact and in determining this the court may disregard the form of any transaction and the separate corporate existence of any participant.

Joint and several liability

_____(3) Where more than one person is found liable or has admitted liability for a particular breach of trust under this Act, those persons are jointly and severally liable.

Contribution

_____(4) A person who is found liable, or who has admitted liability, for a particular breach of a trust under this Act is entitled to recover contribution from any other person also liable for the breach in such amount as will result in equal contribution by all parties liable for the breach unless the court considers such apportionment would not be fair and, in that case, the court may direct such contribution or indemnity as the court considers appropriate in the circumstances.

RIGHT TO INFORMATION

Right to information;

_____~~39.~~-(1) Any person ~~having a lien or~~ who is the beneficiary of a trust under this Act ~~or who is a mortgagee~~ may, at any time, by written request, require information to be provided within a reasonable time, not to exceed twenty- one days, as follows:

from owner or contractor

1. By the ~~owner or~~ contractor, with,
 - i. the names of the parties to the contract,

- ii. the contract price,
- iii. the state of accounts between the owner and the contractor,
- iv. a copy of any labour and material payment bond in respect of the contract posted by the contractor with the owner, and
- v. ~~a statement of whether the contract provides in writing that liens shall arise and expire on a lot-by-lot basis.~~

from contractor or subcontractor

- 2. By the contractor or a subcontractor, with,
 - i. the names of the parties to a subcontract,
 - ii. the state of accounts between the contractor and a subcontractor or between a subcontractor and another subcontractor,
 - iii. a statement of whether there is a provision in a subcontract providing for certification of the subcontract,
 - iv. a statement of whether a subcontract has been certified as complete, and
 - v. a copy of any labour and material payment bond posted by a subcontractor with the contractor or by a subcontractor with another subcontractor.

from owner

- ~~3. By an owner who is selling the owner's interest in a premises that is a home, with,~~

- i. ~~the name and address of the purchaser, the sale price, the amount of the purchase price paid or to be paid prior to the conveyance, the scheduled date of the conveyance and the lot and plan number or other legal description of the premises as contained in the agreement of purchase and sale, and~~
- ii. ~~the date on which a permit authorizing occupancy or a certificate of completion and possession has been issued.~~

from mortgagee or unpaid vendor

~~_____ (2) Any person having a lien or any beneficiary of a trust under Part II may, at any time, by written request, require a mortgagee or unpaid vendor to provide the person within a reasonable time, not to exceed twenty-one days, with,~~

- ~~(a) sufficient details concerning any mortgage on the premises to enable the person who requests the information to determine whether the mortgage was taken by the mortgagee for the purposes of financing the making of the improvement;~~
- ~~(b) a statement showing the amount advanced under the mortgage, the dates of those advances, and any arrears in payment including any arrears in the payment of interest; or~~
- ~~(c) a statement showing the amount secured under the agreement of purchase and sale and any arrears in payment including any arrears in the payment of interest.~~

by trustee or workers' trust fund

~~_____ (3) The trustee of a workers' trust fund may at any time by written request require any contractor or subcontractor to permit the trustee, within a reasonable time after making the request, not to exceed twenty-one days, to inspect the payroll records of all workers who are beneficiaries of the fund, and who have supplied labour to the making of the improvement, and who are employed by the contractor or the subcontractor.~~

respecting publication of certificate of substantial performance

~~_____ (4) A contractor shall, upon written request whenever made to the contractor by any person, within a reasonable time furnish in writing to the person the date of publication and the name of the construction trade newspaper in which a copy of a certificate of substantial performance has been published under subsection 32(1).~~

Liability for failure to provide information

____(5) Where a person, who is required under subsection (1), (2), (3) or (4) to provide information or access to information, does not provide the information or access to information as required or knowingly or negligently mis- states that information, the person is liable to the person who made the request for any damages sustained by reason thereof.

Order by court to comply with request

____(6) Upon motion, the court may at any time, whether or not an action has been commenced, order a person to comply with a request that has been made to the person under this section and, when making the order, the court may make any order as to costs as it considers appropriate in the circumstances, including an order for the payment of costs on a solicitor-and-client basis.