BUILDERS' LIEN ISSUES

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The Builders' Lien Act, S.S. 1984-85-86, c. B-7.1 (the "Act") is one of those pieces of legislation that you see often enough but that in practice is not always understood that well. This is not for a lack of trying on the part of practitioners, but rather in some degree has to do with the unique nature of the legislation and the various remedies and provisions under the Act. While I do not profess to have all of the answers, I hope I can shed some light on some of the issues you might face in dealing with the Act and some of the common misperceptions of the Act.

I. Overview of the Act

Before turning to some practical considerations and misconceptions, it is useful to go through a quick overview of the Act. While there are provisions dealing with the practice and procedure of dealing with lien actions, the real meat of the legislation as far as solicitors would usually be concerned are found in three main areas: the trust provisions, the lien provisions, and the holdback provisions.

One word of caution before embarking on this exercise--one must pay careful attention to the specific definitions in the legislation, for example contract and subcontract are specifically defined terms and various timelines and requirements under the Act turn on which of those two your are talking about.

A. The Trust Provisions

Part II of the Act sets out the various provisions dealing with three main types of statutory trusts, namely the owner's trust, the contractor's trust, and the subcontractor's trust. Regardless of type of trust involved, if you have non-monetary consideration for part of the agreement, the value of that consideration is deemed to form part of the value of the amount available for the respective trust. For example, if an owner contracted with a contractor to build a building for $1,000,000 with a discount for early payment of 5% (i.e. if the owner paid within a shorter time frame the contract price would be reduced), the owner's trust would be $1,000,000.

Another important consideration is that set off is allowed between the trustee and whomever they have contracted with. In other words, the trustee is allowed to claim against (and therefore effectively reduce) the amount of the trust for amounts that its

payee may owe or be liable to the trustee for. This is, however, subject to the obligation to maintain a holdback.

Every payment a trustee makes to a party they are liable to pay reduces the trust obligations to all beneficiaries. For example, if a contractor has subcontracts with several subcontractors (or subtrades), the overall contract price would be a trust held for all the subcontractors. Every payment that contractor rightfully made to any one of those subcontractors would correspondingly reduce the trust obligations of the contractor. However, again, this is subject to the obligation to maintain a holdback.

A significant factor that some overlook is who may be liable for breach of the trust provisions. This liability not only extends to directors and officers, but can also apply to any person who has effective control of the corporation or its relevant activities. This could extend to, for example, a parent company, as the Act specifically allows a Court to ignore the form of the transaction and any separate corporate existence. The Act even provides for quasi-criminal liability as well.

The trust provisions themselves are a remedy separate and apart from the lien remedy. This is made clear in that the Act specifically states that the trust provisions are not affected by the expiry of the time to register a lien. That being said, it is important to note that the trust remedy has a one year limitation period from when the contract is abandoned or completed.

At one time, there was essentially one trust under the Act for the benefit of all in the construction pyramid. However, the Act now provides for three separate trusts, namely the owner's trust, the contractor's trust, and the subcontractor's trust. Although the writer has seen several pleadings assert that in effect there is one trust, the Act itself seems to distinguish between the three types of trusts.

The owner's trust is held for the benefit of the contractor or contractors (there can be more than one entity that has a direct contract with the owner). The trust attaches to all monies received by the owner for the financing of an improvement exclusive of the purchase price of the land. This trust also attaches to the owner's own capital or money in hand that can be used to pay amounts owing to the contractor. If an owner sells the improvement, the sale price less any amounts required to payout encumbrances or sale expense is a trust for the contractor.

The contractor's trust applies to amounts owing to the contractor whether they are due or payable or received by the contractor. The word "payable" suggests that even though payment may not yet be due under the strict terms of the contract, if the contractor has earned it, the value of what was earned is part of the trust. This trust is held for the benefit of the subcontractors, the suppliers who provided material to the

contractor, and the labourers employed by the contractor who are working on the specific improvement.

The subcontractor's trust is essentially the same in form as the contractor's trust, with the exceptions being that the subcontractor becomes the trustee and the beneficiaries are those in some form of contractual relationship with the subcontractor.

B. The Lien Provisions

The lien provisions grant those providing services or materials to an improvement a claim on the improvement. The lien rights arise as soon as the work or materials are provided to the improvement. The lien is a charge on the estate or interest of the owner, as well as a charge on the materials provided, up to the value of what was provided but remains unpaid.

A joint owner is generally bound by a lien as well, even if they had no direct dealings with the lien claimant. The joint owner can, however, avoid that binding effect if, before the lien first arises (i.e. first services or materials are provided to the improvement), actual notice is given to the lien claimant that the joint owner assumes no responsibility for the improvements to be done.

Landlords are also bound if before work starts they get a written notice from the contract. However, if the landlord responds in writing in 10 days advising that they will not accept responsibility for the improvement, then the landlord is not bound. Even where the landlord is bound, they are only liable up to the value of holdback that the owner is to maintain. Where a landlord accepts responsibility under this provision of the Act, they cannot avoid the lien by simply having title revert back to them.

Liens on condominiums depend on whether the work was done on a unit or common property. For the former, the lien can be registered against the owner's title and forms a charge against both the unit and the share of the common property reflected on title. For the latter, the lien can be registered against all titles issued under the condominium plan.

The lien is a charge on the holdback as well as on any additional amount owed by the payer to the payee against whom a lien is claimed.

C. The Holdback Provisions

Each payer in the construction pyramid is required to holdback 10%. The 10% is calculated to be the greater of the actual value of what has been provided and the amount of any payment already made by the payer. This obligation applies regardless of any payment terms under any contract or subcontract. A mortgagee can maintain the

holdback on behalf of the owner and that satisfies the owner's obligation to maintain a holdback.

The holdback is inviolable meaning it cannot be used by the owner to complete the project or remedy a default if the contractor fails to complete or defaults on the contract. If a payer on a contract fails to release the holdback when required to do so, they can be liable to the payee for any damages they suffer as a result. An owner is personally liable to each lien claimant who has a valid lien claim in the proportion that the lien claimant is entitled to the holdback. For example, if you had a holdback of $30,000 and had valid three lien claimants each with liens of $30,000 (for a total of $90,000), the owner would be personally liable to each lien holder in the amount of $10,000.

Although all payers are required to retain the holdback, the owner is the only one required to maintain a holdback trust account. The writer is of the view that in many instances this is not in fact done, even on large projects. In addition, there are some specific directions as to how that account should be dealt with, but, again, the writer suspects those are not followed all that often. The requirement does not apply to the Crown or where the contract is in relation to a house, four-plex or condominium (all as defined under the Act) or a contract with an architect or engineer.

Any interest that might accumulate on the holdback trust account is to be dealt with according to the terms of the contract, something that is not always dealt with expressly in contracts. In those cases, the default under the Act is that the interest goes to the owner. However, if there are unpaid lien claimants after the holdback has been paid out, any accrued interest would be distributed to those lien claimants first.

Related to the holdback provisions is the concept of the written notice of lien. This is a separate concept from the claim of lien and there is a separate form for it. There is in theory an argument that can be made that serving a claim of lien is equivalent to serving a written notice of lien (section 100 of the Act talks about irregularities), however, rather than test that argument, the better practice is to serve both of claim of lien and a written notice of lien. While the claim of lien stakes the lien claimant’s claim to the holdback, the written notice of lien has the effect of freezing all funds on the project unless the payer who is served retains an amount equal to the lien claim.

There is a very important distinction between a claim of lien and written notice of lien that must be kept in mind when dealing with them and in potentially settling a dispute. Once a claim of lien is discharged, it cannot be revived. A written notice of lien, however, can be withdrawn and served again any number of times.

II. Practical Considerations

With that background in mind, I now want to turn to how some of that plays out in practice and some ways that you might want to consider in dealing with lien issues and complying with the Act.

As a preliminary comments--and as mentioned before--many times an owner does not actually maintain a separate trust account for the holdback. While this may not apply in residential situations, it does apply elsewhere.

A. Direct Payment

One provision that can prove somewhat useful is section 47 of the Act. It allows a payer to pay a lien claimant directly. The payer has to give to the proper payer of the lien claimant three days notice of its intention to do so. If the proper payer fails to object, the payer can make the payment without jeopardy and the proper payer cannot complain. To illustrate, if an owner gives a contractor three days notice that it is going to pay a lien claimant and the contractor fails to object, the owner is at liberty to pay the lien claimant and the contractor is then unable to challenge that payment. It is important to keep in mind, though, that any such payments do not reduce the amount of the holdback to be maintained.

B. Substantial Completion

This is an important concept under the Act as it generally triggers when a payer is entitled to release the holdback (the other triggers being abandonment or completion as defined under the Act). Substantial completion can be certified by a payment certifier (defined to be an architect, engineer or other person on whose certification payment is made) or, if none, the owner (if talking about the contract) or the owner and contractor jointly (if talking about a subcontract) certifying that the work is substantially complete as defined under the Act. Substantial completion is when the work is able to be or is being used as intended and the cost to complete or remedy a defect is less than or equal to 3% of the first $500,000 in contract value, 2% of the next $500,000 of contract value, and 1% of the remaining contract value.

1. Payment Certified Contracts/Subcontracts

For those contracts that have a payment certifier, they are required, when requested, to determine within a seven day period whether the contract is complete as defined in section 3 of the Act or not. If they determine to issue a certificate of substantial completion, they then have to deliver that certificate to the party making the request, as well as anyone else who requested in writing to get a copy of the certificate. But the obligations do not end there, as the payment certifier has to post the certificate on a

prominent spot on the job site. This is an important step that has to be taken, but, in some instances is not. The effect of not following this mandatory provision (i.e. that the certificate be posted) is such that whoever fails to post the certificate is liable to those who suffer loss (for e.g. someone who missed out on filing a lien). So the prudent advice is to make sure the certificate is posted on the job site. One job site that it may not be done a lot on is a house. This is a simple thing to be done and the writer is aware of some whose practice it is to instruct their builder clients or owners to post it on the front door of the house.

You may think that once you have the certificate, that is the final word. Alas it is not, as the Act allows for an arbitrator or the Court to come to a different conclusion. If a party takes the issue of substantial completion to arbitration or the Court, any decision rendered on the point has to be delivered in the same manner as the certificate of substantial completion.

The actual date of substantial completion is the date the certificate is signed or the decision is rendered, unless, of course, the certificate or decision specifically says it is another day.

However, the date of substantial completion is perhaps not as critical as the time of delivery of the certificate or decision. It is this date that starts the clock running and which ultimately determines when you can release the holdback. It is important to note that, where you are delivering the certificate to several people, it is when the last person receives the notice that the clock starts to run

2. Non-payment Certified Contracts/Subcontracts

For non-payment certified contracts, the trigger is when the contract is complete (defined under section 4 to be the lesser of $1000 or 1% of the contract value) or abandoned. This is a determination that your client must make and has to be reasonably certain about. If there is any doubt, it could have a serious impact on your client down the road, particularly if they released the holdback too soon, as that could result in personal liability for them.

On the issue of abandonment, Courts have consistently held this is a question of fact in each set of circumstances. Courts have held that the mere passage of time does not equate to abandonment. Further, cessation of work does not necessarily mean the contract has been abandoned. Rather one must look at the evidence to determine whether the work was abandoned or not.

3. Two Holdbacks?

Believe it or not, there can be two holdbacks on the same contract. This arises because, at substantial completion, obviously the job is not 100% complete. There is still additional work that needs to be done. What can be released 40 days after substantial completion is the holdback in relation to work done up to substantial completion. Because work is still ongoing on the contract after substantial completion, the requirement to maintain a holdback still applies. In some provinces, these holdbacks are referred to as the "major lien fund" (i.e. the holdback for work done up to substantial completion) and the "minor lien fund" (i.e. the holdback for work done after substantial completion). This latter fund is only releasable 40 days after the contract is complete or abandoned.

4. Late Registered Liens

In what could be described as an effort to keep Saskatchewan unique, section 49 initially takes away, but then gives you something back. Subsection 49(5) specifically allows for registration of liens beyond the typical 40 day period, something distinctly Saskatchewan, as the writer is unaware of a similar provision in any other Canadian jurisdiction. Although limited in what is attached, nonetheless subsection 49(5) still can create wrinkles for you and it is something you should be aware of in advising clients.

Although not specifically dealt with under the Act, but related to this unique provision, is the concept of sheltering. Courts have allowed lien claimants who have not registered or who have registered late to, as they say, "ride the coattails" of those who did register and registered in the 40 day period.

5. General liens and liens on condominium properties

General liens allow a party to file a lien where they have supplied labour and material to several parcels of land but are unable to discern what the exact amounts for each parcel are. A general lien can be discharged with respect to one or more parcels and still be valid for the remaining parcels. Practically speaking, you may be able to negotiate a discharge of a general lien for payment of a pro rata amount, particularly since subsection 56(3) allows you to apply to the Court to obtain that relief. Although the Act does not specifically address it, similar argument could likely be made in relation to liens on condominium properties, i.e. a lien on an individual unit for work done to the common area could be discharged for payment of a proportionate amount.

6. Things to do/consider before release of funds

Before you advance any funds on a building project, regardless of what stage it is at, you should do a search of title. The Mortgages Procedures Practice Checklist advises

to do a search prior to registration of your mortgage, post registration, and, perhaps most importantly in the context of builders' liens, prior to disbursements. This latter point is especially important because any advances made prior to the registration of a lien are generally fine, subject of course to any possible arguments under the trust provisions of the Act. With the advent of registration time done to seconds, it may be important to record the time the actual disbursements are made, as well, as that could be critical in determining whether an advance was made before or after registration of the lien.

From the perspective of the lien claimant, this is where it can become important to not only register a claim of lien but to serve a written notice of lien as well. Registration of the lien is subject to the vagaries of the land titles registration system and the lien is only actually registered when it goes on title. Because of the possible delays in registration time, there could be advances made while your lien is sitting in the registration queue. A written notice of lien, however, has immediate effect once it is delivered to the payer or mortgagee and the Act specifically says any advances made in the face of a written notice of lien lose priority to the lien. Because of this, it is also likely prudent to check with the mortgagee as to whether they have received any written notices of lien prior to actually disbursing any advances.

Another point to consider is the trust conditions you agree to, whether you are acting for the builder or the owner. For example, technically, it is not sufficient for an owner to rely on a trust condition given by the lawyer for the builder that they will maintain the holdback trust account. That obligation is squarely on the shoulders of the owner and in order for the owner to protect themselves, they should have control over that account. Therefore any trust conditions should clearly deal with who is responsible for maintaining the holdback and when and how it will be released. Further, your trust conditions need to consider the trust provisions of the Act.

On a related note, you should be sure that your trust conditions address the issue of complying with the Act. The Act is express (section 99) in that you cannot contract out of the Act. If your trust conditions do not deal with the Act, you need to be aware of the holdback and trust obligations imposed on your client. You also have to be sure that your trust conditions do not put you offside the Act in terms of, for example, payment of progress payments that ignore the holdback requirements.

Something else that arises is something akin to a progressive release of holdback. What happens is that, with each progress payment, the solicitor actually pays out part of the holdback, usually the amount that was held back on the prior advance but only if 40 days had passed since then. The writer has heard anecdotally that this happens many times and there are a number of practitioners who are engaged in this practice, some even being quite adamant there is nothing offside about it. However, that practice is

clearly offside the express provisions of the Act regarding maintenance and release of the holdback. As mentioned previously, the holdback is to be maintained until substantial completion, abandonment or completion, as the case may be. The only time something like progressive release of holdback is contemplated is on large contracts under section 46 of the Act. The writer is aware that some other provinces are looking at changing their legislation to allow for progressive release of holdbacks, but that is not the law in Saskatchewan. Although practitioners may have avoided any issues in engaging in the progressive release of holdbacks, it really is only a matter of time before a problem arises and a lawyer finds themselves behind the proverbial eight ball.

III. Conclusion

Although not intended to be a thorough review of builders liens, it is hoped this paper has helped refresh your memory in some areas and alert you to some things to consider in your practice.

On a final note, several senior members of the bar have always been accommodating to my calls and questions, and, in keeping with that tradition, I am always happy to talk to someone about an issue they are facing, even if for no other reason than to be a sounding board.

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