



## The Trust

- I. Nature and Purpose of the Trust [§8.1]**
- II. The Builders Lien Act Trust Provisions [§8.2]**
- III. Monies Subject to the Trust [§8.3]**
  - A. General [§8.4]
  - B. The Requirement That Monies Be "Received" [§8.5]
  - C. Monies Not Impressed with the Trust [§8.6]
  - D. Garnishment and Money in Court [§8.7]
- IV. Trustee's Rights and Responsibilities [§8.8]**
- V. The Trust Beneficiary [§.9]**
- VI. Breach of Trust [§8.10]**
  - A. General [§8.11]
  - B. Quasi-Criminal Consequences of Breach [§ 8.12]
  - C. Civil Consequences of Breach [§8.13]
  - D. Lender's Liability and the Constructive Trust [§8.14]
  - E. Subrogated Trust Claims [§8.15]
  - F. Limitation Periods [§8.16]

## I. NATURE AND PURPOSE OF THE TRUST [§8.1]

One of the main objectives of the *Builders Lien Act* is to ensure that monies flowing between parties within the construction pyramid are not diverted and used for purposes unrelated to the construction project. The Act ensures this object by creating a statutory trust in favour of certain parties within the construction pyramid and imposing penalties where trust monies are used for other than satisfying unpaid beneficiaries.

The Act defines the circumstances in which a trust arises and provides statutory protection for trust monies in the event of the bankruptcy of a trustee, attachment proceedings by non-beneficiaries, claims by purported assignees of monies due under a contract or subcontract, or diversion of trust monies to uses incompatible with the objectives of the Act.

The rights of a trust beneficiary are in addition to its lien rights under the Act. The right to assert a trust claim is independent of the right to assert a valid lien claim. Thus, if for any reason a party otherwise entitled to a claim of lien fails to assert it properly or in a timely manner, or if the lands and improvement are not lienable (for example, most federal lands), nevertheless a trust claim may be made where the party is a trust beneficiary under the Act (*Crane Canada Ltd. v. McBeath Plumbing & Heating Ltd.* (1965), 54 W.W.R. 119 (B.C.S.C.), and *Engineering & Plumbing Supplies Ltd. v. Seaboard Excavating Ltd.* (1988), 29 B.C.L.R. (2d) 309 (Co. Ct.)).

## II. THE BUILDERS LIEN ACT TRUST PROVISIONS [§8.2]

The trust sections of the Act are s. 10 ("Contract money received constitutes trust funds"), s. 11 ("Certain applications of trust fund deemed not to be appropriation or conversion), s. 12 ("Crediting of money earmarked for particular improvement"), s. 13 ("Garnishment and money in court"), and s. 14 ("Limitation period").

Related sections include s. 5(2)(b) (holdback trust account) and s. 42 (assignments void as against trust). To an extent not inconsistent with the provisions of the Act, the general law of trusts applies.

## III. MONIES SUBJECT TO THE TRUST [§8.3]

### A. GENERAL [§8.4]

Section 10 of the *Builders Lien Act* provides that "[m]oney received by a contractor or subcontractor on account of the price of the contract or subcontract constitutes a trust fund for the benefit of persons engaged in connection with the improvement by that contractor or subcontractor and the contractor or subcontractor is the trustee of the fund"

(s. 10(1)). And until all trust beneficiaries are paid, the contractor or subcontractor "must not appropriate any part of the fund to that person's own use or to a use not authorized by the trust" (s. 10(2)).

However, s. 10(1) and (2) do not apply to money received by an architect, engineer, or material supplier (s. 10(4)).

Monies paid into a holdback account by, or on behalf of, the owner, are held in trust for the contractor subject to payment of all liens arising under the contractor from whom the holdback was retained (s. 5(2)). Monies paid into court by way of interpleader may be impressed with the trust (*British Columbia Buildings Corp. v. Arbour Contracting Ltd.* (1996), 17 B.C.L.R. (3d) 135 (S.C.)). Monies paid into court as security to cancel a lien under s. 24 are subject to the trust and any sum in excess of proven liens is available to trust beneficiaries. Whether funds paid to the trust account of a lien claimant's lawyer, and held on undertakings, are subject to the trust will depend on the terms of the agreement under which the funds are held.

## **B. THE REQUIREMENT THAT MONIES BE "RECEIVED" [§8.5]**

The Act requires that monies be "received" before becoming impressed with the statutory trust. The requirement is subject to the special case of monies that are:

- (1) paid into the holdback account (s. 5(2)(b)),
- (2) paid into court pursuant to the Act (s. 13(5)), and
- (3) held on a constructive trust.

It is not required, however, that the contractor or subcontractor physically receive the monies to impress them with a statutory trust, and it is sufficient if the monies are paid into court in certain circumstances.

In *Modular Products Ltd. v. Aristocratic Plywoods Ltd.* (1974), 42 D.L.R. (3d) 617 (B.C.C.A.), monies paid into court by a contractor pursuant to a third party demand by Revenue Canada for excise and income taxes remained impressed by the trust in favour of the subcontractors. See also *Minneapolis-Honeywell Regulator Co. v. Empire Brass Manufacturing Co.*, [1955] S.C.R. 694; *Re Northwest Electric Ltd.*, [1973] 3 W.W.R. 156 (B.C.S.C.); *Cronkhite Supply Ltd. v. British Columbia (Workers' Compensation Board)* (1976), 1 B.C.L.R. 142 (Co. Ct.), affirmed in part (1978), 8 B.C.L.R. 54 (C.A.), affirmed, [1979] 2 S.C.R. 27; and *Crane Canada Ltd. v. McBeath Plumbing & Heating Ltd.* (1965), 54 W.W.R. 119 (B.C.S.C.).

In *A & M Painting Contractors Ltd. v. Byers Construction Western Ltd.* (1981), 28 B.C.L.R. 43 (C.A.), monies paid into court by the owner, pursuant to attachment

proceedings, were held to be "received" and were impressed with the trust in favour of subcontractors. Section 13 codifies this result:

#### **Garnishment and money in court**

**13** (1) In the case of money owing to a contractor or subcontractor that would, if paid to the contractor or subcontractor, be subject to a trust under section 10, the money, if it is paid into court under an attachment under the *Court Order Enforcement Act*, is subject to a trust as if it had been paid to the contractor or subcontractor, and the interest of the garnishor is subordinate to the interest of the beneficiaries of the trust.

If money is paid into court pursuant to the Act, by an owner, contractor, or subcontractor, it then "becomes or remains subject to the trust" (s. 13(5); see also *British Columbia Buildings Corp. v. Arbour Contracting Ltd.* (1996), 17 B.C.L.R. (3d) 135 (S.C.)).

In *Wall Brothers Construction Co. v. Canson Enterprises Ltd.* (1986), 70 B.C.L.R. 243 (C.A.), the Court held that if monies are paid on account of a contract, they will be deemed to be "received" by the contractor, notwithstanding that the monies were actually paid to or received in the contractor's account by someone other than the contractor.

Monies retained by the owner, other than in the holdback account, are not generally impressed with the statutory trust (*Wall Brothers Construction*).

However, in some instances, monies that are due and payable, but retained by or on behalf of an owner, have been held to be subject to a non-statutory constructive trust in favour of the contractor or subcontractor. In *Atlas Cabinets & Furniture Ltd. v. National Trust Co.* (1990), 45 B.C.L.R. (2d) 99 (C.A.), the Court held that the unadvanced portion of a construction mortgage was impressed by a "remedial constructive trust" in favour of subcontractors to prevent the "unjust enrichment" of a mortgage lender (see also *Voth Brothers Construction (1974) Ltd. v. National Bank of Canada* (1988), 32 C.L.R. 1 (B.C.C.A.)). In most cases, holdback monies not paid into the owner's holdback account will not be deemed to be held on a constructive trust, and they will not have been "received" so as to be impressed with the statutory trust.

A constructive trust may be established where there is proof of enrichment, a corresponding deprivation, the absence of any juristic reason for the enrichment and corresponding deprivation, and an element of injustice (*Atlas Cabinets and Furniture Ltd. v. National Trust Co.*; see also *Winroc Corp. v. Colwood Contracting Ltd.* (1996), 30 C.L.R. (2d) 31 (B.C.S.C.), and the cases discussed at §8.13 and §8.14).

Monies paid to a trustee's assignee remain impressed with the trust (s. 42(4); see also *Groves-Raffin Construction Ltd. v. Canadian Imperial Bank of Commerce* (1975), 64 D.L.R. (3d) 78 (B.C.C.A.)). Monies paid by an owner to a surety for the completion of the work of a bankrupt contractor are impressed with the trust in favour of beneficiaries of

the insolvent contractor (*Commercial Union Assurance Co. of Canada v. Surrey (City)* (1997), 38 B.C.L.R. (3d) 389 (C.A.), leave to appeal refused (18 September 1997), 26006 (S.C.C.)).

A person who receives trust monies in respect of a particular improvement must credit them against any debt due to that person in respect of that improvement and not against any other unrelated or general debt owed by the payor (s. 12).

### **C. MONIES NOT IMPRESSED WITH THE TRUST [§8.6]**

Monies received by an architect, engineer, or material supplier are not subject to the trust (s. 10(4)). This provision is compatible with the limited reach of the builders lien legislation and the fact that the Act does not afford liens in favour of persons who perform or provide work, or supply materials, to an architect, engineer, or material supplier (s. 2(2)).

Subject to the foregoing comments, monies must not only be "received" but must be received "on account of the price of the contract or subcontract" (s. 10(1)). Monies received by a trustee as a result of its inadvertent overcharging would not be considered received "on account of the price of the contract" and would not be subject to the trust (*Vancouver City Savings Credit Union v. Elliott* (1991), 49 C.L.R. 294 (B.C.S.C.)).

A beneficiary's entitlement to trust monies is limited to the amount due and owing to the beneficiary (*British Columbia Hydro & Power Authority v. Hallcraft Construction Co.* (1986), 6 B.C.L.R. (2d) 74 (S.C.)).

### **D. GARNISHMENT AND MONEY IN COURT [§8.7]**

Money held in the owner's holdback account is not subject to garnishment (s. 13(4)). Section 13(1) provides that in the case of monies that would, if paid, be subject to the trust when paid into court pursuant to attachment proceedings, the monies are subject to the trust and "the interest of the garnishor is subordinate to the interest of the beneficiaries of the trust". A garnishee in such a case must, at the time of payment into court, file in the court registry "a notice in the prescribed form and deliver a copy of the notice to the garnishor" (s. 13(2)) (Form 4 of the Builders Lien Forms Regulation, reproduced at FP 20 in the "Forms and Precedents" section of this Manual). Where a notice is filed, the registrar is prevented from paying monies out of court without a further court order (s. 13(3)).

## **IV. TRUSTEE'S RIGHTS AND RESPONSIBILITIES [§8.8]**

Until all trust beneficiaries are paid, the contractor or subcontractor is prohibited from appropriating any part of the trust monies "to that person's own use or to a use not authorized by the trust" (s. 10(2)). A trustee who does so commits a breach of trust and commits an offence (s. 11(1) and (2)).

The Act, however, codifies previous common law to the effect that the trustee may retain an amount equal to amounts paid by the trustee in respect of work or materials supplied to the project, and may use trust funds to repay a loan to a third party for funds used to pay "for all or part of work or material supplied". In doing so, a trustee does not commit "an appropriation or conversion" that contravenes the trust provisions of the Act (s. 11(4)).

The Act clarifies the earlier common law and provides that commingling *simpliciter* of trust monies with other monies, by a contractor or subcontractor, does not constitute a breach of trust under s. 10(1) or a contravention of s. 10(2) of the Act (s. 11(7)).

Contractors and subcontractors have a right to set off and deduct from payments of trust monies, monies in respect of counterclaims against the beneficiary. It is doubtful that a contractor could successfully establish an equitable set-off to a trust claim by asserting a cross-claim arising out of payments made on behalf of the beneficiary on an unrelated project (*J.W. Price Construction Ltd. v. Elan Construction Ltd.*, 2001 BCSC 1125). The right to a set-off is subject to the trustee's obligation to continue to retain all trust monies until the counterclaim is proven and subject to lien claims (*United Metal Fabricators Ltd. v. Voth Brothers Construction (1974) Ltd.* (1987), 20 B.C.L.R. (2d) 274 (C.A.)). The trustee should act in a timely manner in formalizing its claim to set off by way of counterclaim (*Henry Electric Ltd. v. Farwell* (1986), 5 B.C.L.R. 273 (C.A.), leave to appeal refused (1987), 75 N.R. 160 (note) (S.C.C.)).

A trustee whose own workers supply work to the improvement, may pay trust monies to its employees qua beneficiaries, and the trustee is not bound by the one to one distribution rule under s. 11(4)(a).

A trustee is not obliged to pay out all trust funds during the course of the project on a pro rata basis. A trustee has the discretion to pay out for permitted purposes, trust funds in any manner it deems fit (*Minneapolis-Honeywell Regulator Co. v. Empire Brass Manufacturing Co.*, [1955] S.C.R. 64, and *Inlaid Floor & Supply Co. (Nanaimo) v. Bastion Construction Ltd.* (1985), 65 B.C.L.R. 69 (C.A.)).

Trust funds used by a contractor to pay its own overhead costs (such as builder's risk insurance costs, audit fees, telephone costs, and personnel agencies for employees) will be considered appropriations "to that person's own use or to a use not authorized by the Act" (*Dietrich Steel Ltd. v. Shar-Dee Towers (1987) Ltd.* (1999), 45 C.L.R. (2d) 178 (Ont. C.A.)). Performance bond premiums, liability and group insurance costs, and third-party remittances (employer health tax, Canada Pension Plan contributions, and employment insurance premiums) not falling within the definition of "wages" (s. 1(1)) will generally be considered overhead expenses (*S.E. Rozell & Sons v. Groff* [2000] O.J. No. 701 (S.C.)).

However, a discretion to disburse trust funds is subject to the general trust law rights of unpaid beneficiaries. In *Re Putherbough Construction Co.* (1958), 37 C.B.R. 6 (Ont. S.C.), the Court held that equity required a trustee in bankruptcy, where trust funds were

insufficient to pay the total claims of the creditors of the bankrupt's estate, to pay the remaining funds rateably among creditors of the same class. Rateable payments out of trust monies may still lead to trustee's liability, if outstanding trust claims are pending. In *Guaranty Trust Co. of Canada v. Beaumont* (1966), 61 D.L.R. (2d) 286 (Ont. C.A.), an absconding contractor assigned project funds to its trustee who paid out the funds with knowledge of a beneficiary's action to have the true value of its claim determined. The trustee was held not to have acted reasonably in distributing the monies with notice of the plaintiff's claim for the superior share.

## V. THE TRUST BENEFICIARY [§8.9]

A contractor or subcontractor who receives money on account of the price of the contract or subcontract holds those monies in trust "for the benefit of persons engaged in connection with the improvement by that contractor or subcontractor" (s. 10(1)). Privity is the *sine qua non* of the trust relationship between the contractor or subcontractor, and the beneficiary of the trust. A "contractor" means a person engaged by an owner to perform or provide work, or supply material "in relation to an improvement" but does not include a worker (s. 1). A "subcontractor" means a person engaged by a contractor or another subcontractor to perform or provide work, or supply material, but does not include "a worker or a person engaged by an architect, an engineer or a material supplier" (s. 1).

A "worker" means an individual engaged "for wages in any kind of work, whether engaged under a contract of service or not" but does not include an architect or engineer, or a person engaged by an architect or engineer (s. 1). Under the former Act, an owner could successfully maintain an action for breach of trust against an absconding contractor in relation to the owner's excess costs to complete the project (see *Mann v. Pain*, [1997] Civ. L.D. 200 (B.C.S.C.)). Now, unless the owner is "engaged" by a contractor or subcontractor to supply labour to complete an improvement, the owner cannot assert rights as a beneficiary under the trust (s. 10).

Under the former Act, subcontractors became beneficiaries only where they supplied work or materials "on" the site of the improvement, or if the supply of work and materials was integral and necessary to the improvement (*Kettle Valley Contractors Ltd. v. Cariboo Paving Ltd.* (1986), 1 B.C.L.R. (2d) 236 (C.A.)). Thus, truck suppliers and persons providing room and board for workers were held under the former Act not to qualify as trust beneficiaries (*Cam Cement Contractors Ltd. v. Royal Bank* (1973), 38 D.L.R. (3d) 427 (B.C.C.A.); see also *Re Northwest Electric Ltd.*, [1973] 3 W.W.R. 156 (B.C.S.C.)). Whether the Act enlarges the class of potential beneficiaries to include those who supply labour and materials "in connection with" but not "on" an improvement will be determined as the case law develops. Whereas trust rights conferred under builders lien legislation should be liberally interpreted, provisions defining the class of persons who may constitute trust beneficiaries have been strictly interpreted (*Enermax Fabricators Ltd. v. David L.S. Pearce & Associates Ltd.* (1986), 7 B.C.L.R. (2d) 347 (C.A.); and *Ace Lumber Ltd. v. Clarkson Co.*, [1963] S.C.R. 110).

A material supplier may be a trust beneficiary qua "contractor" or "subcontractor" (s. 1). The trust claims of material suppliers are limited to the price of materials supplied on or before the date of a progress payment paid to the trustee (*Van Vliet Construction 1988 Ltd. v. Jaeger* (1998), 50 B.C.L.R. (3d) 147 (S.C.), affirmed (1998), 60 B.C.L.R. (3d) 220 (C.A.)); see also *Metro Aluminum Products Ltd. v. Civic Glass Systems Inc.* (1996), 31 C.L.R. (2d) 194 (B.C.S.C.). The same should apply *mutatis mutandis* to the trust claims of subcontractors for the supply of services (see *Metro Aluminum Products*).

If a person pays trust monies to a beneficiary in relation to a particular improvement, the beneficiary must credit the amount received against the debt owed to it in relation to that improvement (s. 12). Thus, the trust beneficiary cannot unilaterally allocate trust payments to amounts owed for other improvements. If it does so, it may risk its lien rights (*Metro Aluminum Products*). A contractor acting in the capacity of trustee will be in breach of trust if it pays trust monies to creditors on unrelated projects (*McConnell Air Conditioning & Refrigeration Services (B.C.) Ltd. v. York Sheet Metal Ltd.* (1985), 15 C.L.R. 308 (B.C. Co. Ct.)). Section 12 codifies prior case law that held that the rule in Clayton's Case (that is, that monies received must be appropriated first to the oldest outstanding account between the payor and the payee) does not apply to the *Builders Lien Act* trust (see *Tempo Building Supplies Ltd. v. Villa Cathay Care Home Society* (1980), 67 B.C.L.R. 44 (Co. Ct.)). It is implicit in the Act that a beneficiary receiving trust monies will have its lien rights extinguished to the extent of the payments made (*Ross Gibson Industries Ltd. v. Greater Vancouver Housing Corp.* (1985), 67 B.C.L.R. 55 (C.A.); *J.W. Price Construction v. Costco Wholesale Corp.*, 2000 BCCA 22).

## **VI. BREACH OF TRUST [§8.10]**

### **A. GENERAL [§8.11]**

A breach of trust may give rise to civil liability, a quasi-criminal offence, or a criminal offence. It is well established that noncompliance with a statutory trust will attract civil liability (*Minneapolis-Honeywell Regulator Co. v. Empire Brass Manufacturing Co.*, [1955] S.C.R. 694; see also *Trilec Installations Ltd. v. Bastion Construction Ltd.* (1982), 135 D.L.R. (3d) 766 (B.C.C.A.)). Section 10 of the Act creates a distinct cause of action, and lien claimants, whether or not entitled to a declaration of lien, may pursue a claim for breach of trust (*Dominion Electric Protection Co. v. Beaudoin Construction Co.* (1963), 5 C.B.R. (N.S.) 72 (Ont. H.C.); *Okanagan Blasting v. Contech Enterprises Ltd.* (1983), 50 B.C.L.R. 82 (S.C.); and *Crane Canada Ltd. v. McBeath Plumbing & Heating Ltd.* (1965), 54 W.W.R. 119 (B.C.S.C.)). A breach of trust claim may be pursued in the B.C. Provincial Court (Small Claims Division), subject to its monetary jurisdiction, or in the Supreme Court pursuant to the Supreme Court Rules (*Valley Rite- Mix Ltd. v. Storrie* (1993), 86 B.C.L.R. (2d) 312 (S.C.); *Fraser Sash & Door Co. v. Bevenco Construction Ltd.* (1961), 35 W.W.R. 124 (B.C. Co. Ct.)). See also *Coast Building Supplies Ltd. v. Vancan Drywall Ltd.*, 2001 BCPC 325).

An action for breach of the statutory trust is distinct from an action for breach of duty in tort (*Hub City Supplies v. Total Drywall Ltd.* (1996), 29 C.L.R. (2d) 275 (B.C.S.C.)). The *Builders Lien Act* does not prevent the joinder of trust and lien claims in one action. Further, separate trust and lien actions may be consolidated for trial (Supreme Court Rule 5). The Act is not intended to have extraterritorial application. Thus, proceedings relating to a breach of trust will not lie where the improvement is outside British Columbia (*E.B. Horsman & Son v. Sigurdson* (1979), 13 B.C.L.R. 20 (S.C.); and *Batoni Construction Inc. v. Anthomax Mechanical Ltd.* (1997), 33 C.L.R. (2d) 134 (Ont. C.A.)). An action for breach of the statutory trust is probably a "proceeding under [the] Act" and as such the local venue rule for proceedings applies (s. 27).

Monies paid into court will be retained until potential trust beneficiaries have had an opportunity to establish their claims. The court is under no duty to seek out and identify potential trust beneficiaries, but it will not permit funds to be disbursed without affording an opportunity for potential beneficiaries to establish their rights by action (*Fraser Sash & Door Co. v. Bevenco Construction Ltd.*, and *Canadian Forest Products Ltd. v. 385784 B. C. Ltd.* (1996), 31 C.L.R. (2d) 79 (B.C.S.C. Master)).

An action for breach of trust is maintainable even where:

- (1) a potential lien claimant has failed to file a claim of lien;
- (2) the time limit for filing a claim of lien has expired, or
- (3) a claim of lien is not maintainable, for example, in relation to an improvement on federal Crown land (*Engineering & Plumbing Supplies Ltd. v. Seaboard Excavating Ltd.* (1988), 29 B.C.L.R. (2d) 309 (Co. Ct.)).

A lien claimant, in addition to obtaining a judgment for a share of holdback funds, can maintain a separate action for breach of trust (*G.C. McDonald Supply Ltd. v. Preston Heights Estates Ltd.* (1992), 1 C.L.R. (2d) 157 (Ont. Ct. (Gen. Div.))). However, a trust provision cannot be used to obtain a double recovery, and trust monies received must be credited to the claimant's lien entitlement (*Ross Gibson Industries Ltd. v. Greater Vancouver Housing Corp.* (1985), 67 B.C.L.R. 55 (C.A.); *J.W. Price Construction v. Costco Wholesale Corp.*, 2000 BCCA 22). A trustee will be held to a legal duty to properly account for its use of the trust funds (*Jacobson v. Basile's Developments Ltd.* (1983), 45 B.C.L.R. 199 (S.C.)).

## **B. QUASI-CRIMINAL CONSEQUENCES OF BREACH [§8.12]**

A contractor or subcontractor commits an offence if that person appropriates or converts trust monies in contravention of s. 10 of the Act (s. 11). A person who commits an offence under the Act is liable to a fine of not more than \$10,000 or to imprisonment for a term of not more than two years or both (s. 11(2)). If a contractor or subcontractor is a corporation, a director or officer of the corporation who "knowingly assents to or acquiesces in an offence" under s. 11(1)(a) of the Act by the corporation, "commits the

offence in addition to the corporation" (s. 11(3)). Corporations and their directors, officers, agents, and others will be deemed to have knowledge of the statutory trust (*British Columbia v. D'Sena* (1995), 56 B.C.A.C. 238 (C.A.)).

Section 11(3) of the Act codifies common law cases that impose liability on persons acting in relation to corporate breaches of trust. See, for example, *Henry Electric Ltd. v. Farwell* (1986), 5 B.C.L.R. 273 (C.A.); *Horsman Brothers Holdings Ltd. v. Panton*, [1976] 3 W.W.R. 745 (B.C.S.C.); *Trilec Installations Ltd. v. Bastion Construction Ltd.* (1982), 135 D.L.R. (3d) 766 (B.C.C.A.); *Clarkson Co. v. Canadian Bank of Commerce*, [1966] S.C.R. 513; and *Scott v. Riehl* (1958), 15 D.L.R. (2d) 67 (B.C.S.C.).

The liability of a director or officer for a corporate breach of trust is not vicarious liability. Their liability requires proof either of actual knowledge of the breach or of a reckless indifference to it (*Gough Electric Ltd. v. Baziuk* (1983), 45 B.C.L.R. 269 (Co. Ct.); *West Kootenay Mechanical Ltd. v. Henderson* (1986), 23 C.L.R. 67 (B.C. Co. Ct.); and *British Columbia Ventilating Ltd. v. Intercontinental Environmental Controls Ltd.* (1977), 3 B.C.L.R. 89 (S.C.)). The criteria of knowing assent or acquiescence, on which a director or officer's quasi-criminal liability is founded, has been applied to base claims for civil liability (*West Kootenay Mechanical*).

An "innocent" breach of trust resulting from sloppy bookkeeping may be sufficient to attract liability to directors or officers (*Horsman Brothers Holdings Ltd. v. Panton*; see also *Cemco Electrical Manufacturing Co. v. A. Anthony Ltd.* (1952), 6 W.W.R. (N.S.) 552 (B.C. Co. Ct.)). "Acquiescence" is sufficient to found liability in a corporate director or officer. In *Van Vliet Construction 1988 Ltd. v. Jaeger* (1998), 50 B.C.L.R. (3d) 147 (S.C.), affirmed (1998), 60 B.C.L.R. (3d) 220 (C.A.), a director who acquiesced to a co-director diverting trust monies from corporate subtrades, was found equally liable with a co-director who managed the finances of the corporation. Further, a person who has knowledge of a breach of trust may be held to be a *trustee de son tort*, whether or not a statutory trustee (*Gough Electric Ltd. v. Baziuk*).

It is doubtful that a trustee who acted "honestly and reasonably, and ought fairly to be excused for the breach of trust" may be relieved from personal liability therefore by operation of s. 96 of the *Trustee Act*, R.S.B.C. 1996, c. 464. The *Trustee Act* likely does not apply to a trust created under the *Builders Lien Act*, and any breach of trust there under is prima facie unreasonable (see *Ontario Electrical Construction Co. v. S.I. Guttman Ltd.* (1996), 29 C.L.R. (2d) 146 (Ont. Ct. (Gen. Div.)), affirmed (1997), 104 O.A.C. 232 (C.A.), decided under equivalent Ontario legislation). The burden of proof of establishing a prima facie breach of trust, remains with the party asserting a breach of trust. Upon discharging the burden, the onus shifts to the defendant to account for a11 proceeds (*977724 Ontario Inc. v. Godard* (1997), 33 C.L.R. (2d) 54 (Ont. Ct. (Gen. Div.))).

Section 336 of the *Criminal Code*, R.S.C. 1985, c. C-46, creates the offence of criminal breach of trust. It provides that a trustee of anything for the use or benefit of another person who "converts, with intent to defraud and in contravention of his trust, that thing

or any part of it to a use that is not authorized by the trust is guilty of an indictable offence and liable to imprisonment for a term not exceeding fourteen years". The criminal offence requires proof of a subjective intent to defraud, whereas the quasi-criminal offence created by s. 11 of the Act does not (see *R. v. Brunner* (1960), 32 W.W.R. 478 (B.C.C.A.)).

Quasi-criminal proceedings arising out of a contravention of s. 11(1) of the Act, are governed by the *Offence Act*, R.S.B.C. 1996, c. 338, which provides for summary conviction proceedings in the B.C. Provincial Court (Criminal Division).

### C. CIVIL CONSEQUENCES OF BREACH [§8.13]

Although the Act both creates and circumscribes the statutory trust, and also permits conduct that otherwise might constitute a breach of trust according to the general law, it does not set out civil remedies for breach of trust. Common law and equitable principles apply in determining the civil consequences of a breach of the statutory trust, save as modified by the scheme of the Act.

Generally, in a breach of trust action, the claimant will be required to establish that:

- (1) the claimant is a beneficiary under the Act;
- (2) the trust monies were received by the trustee on account of the price of the contract or subcontract under which the claimant was engaged (or the monies are retained in the statutory holdback account);
- (3) the monies are owing to the claimant for work or materials on the improvement;
- (4) the trustee appropriated the monies for a purpose not authorized by the Act; and
- (5) in the case of a claim against the director or officer of a corporate trustee, he or she knowingly assented or acquiesced to (or were deemed to) the unauthorized use of the trust monies.

A trust claimant, having strictly complied with the requirements for filing a lien, may also participate in the trust (*Kettle Valley Contractors Ltd. v. Cariboo Paving Ltd.* (1986), 1 B.C.L.R. (2d) 236 (C.A.); *Wall Brothers Construction Co. v. Canson Enterprises Ltd.* (1986), 70 B.C.L.R. 243 (C.A.)). Beneficiaries share pro rata in the trust proceeds (*Re Putherbough Construction Co.* (1958), 37 C.B.R. 6 (Ont. S.C.)).

A trust beneficiary may claim against a stranger to the trust, based on a "constructive trust" (*Atlas Cabinets & Furniture Ltd. v. National Trust Co.* (1990), 45 B.C.L.R. (2d) 99 (C.A.); but see *Ram Construction Ltd. v. Standard Trust Co.* (1992) 65 B.C.L.R. (2d) 318 (C.A.)). As to the "knowledge" element required to establish a constructive trust, see *Citadel General Assurance Co. v. Lloyds Bank Canada*, [1997] 3 S.C.R. 805, reversing (1996), 37 Alta. L.R. (3d) 293 (C.A.), and *Gold v. Rosenberg*, [1997] 3 S.C.R. 767,

affirming (1995), 129 D.L.R. (4th) 152 (Ont. C.A.). See also *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217, affirming (1995), 84 O.A.C. 390 (C.A.), regarding the equitable remedy of the remedial constructive trust in the absence of corresponding deprivation and enrichment.

In accordance with general equitable principles, money impressed with a trust can be traced as such into the hands of an assignee, a bank, and directors or employees who appropriated to their own use monies received by trustee corporations. Similarly, a beneficiary will be entitled to an accounting of trust monies. An innocent breach of trust by the controlling director or officer of a corporate trustee can attract civil liability as will his or her reckless indifference or wilful failure to take proper care to prevent third parties from wrongfully appropriating trust monies (*Trilec Installations Ltd. v. Bastion Construction Ltd.* (1982), 135 D.L.R. (3d) 766 (B.C.C.A.)). A non-participating director may not be liable (*Hub City Supplies v. Total Drywall Ltd.* (1996), 29 C.L.R. (2d) 275 (B.C.S.C.)).

Where a director, without knowledge of a corporate breach of the statutory trust, improperly applied trust monies to repay a personal mortgage, it has been held that those monies may be traced in the hands of the director, and the court may impress the mortgaged property with a "remedial" lien in favour of the trust beneficiary (*Instant Lawns Turf Farm (1994) Ltd. v. B & B Landscaping and Maintenance Service Ltd.* (1999), 48 C.L.R. (2d) 9 (B.C.S.C.); see also *Pitkethly & Buzza Ltd. v. Westview Construction Ltd.* (1991), 44 C.L.R. 304 (B.C.S.C.)).

#### **D. LENDER'S LIABILITY AND THE CONSTRUCTIVE TRUST [§8.14]**

Section 11 (4)(b) of the Act provides that:

- (b) if money is loaned to a person on whom a trust is imposed by section 10 and is used to pay for all or part of work or materials supplied, trust money may be applied to discharge the loan to the extent that the lender's money was so used by the trustee, and money so applied is not an appropriation or conversion that contravenes section 10.

Section 11(6) provides that s. 11(4)(b) "does not limit the rights of a lender who, in the ordinary course of business, receives money in good faith from a person on whom a trust is imposed under section 10".

Although lenders and financial institutions are not defined trustees under s. 10 of the Act, they may nevertheless attract civil liability for breaches of trust as a constructive trustee or *trustee de son tort*. A *trustee de son tort* is someone who, as a stranger to the trust, takes on themselves to act as such and to possess and administer trust property (*Selangor United Rubber Estates Ltd. v. Cradock*, [1968] 2 All E.R. 1073 (Ch. Div.)). A bank, having assumed the office or function of trustee, or having administered the trust

funds on behalf of a beneficiary, which deals with the funds in a manner inconsistent with the trust, will be liable on this basis.

A bank may also, as a stranger to the trust, attract civil liability in cases of "knowing assistance" and "knowing receipt". See *Air Canada v. M & L Travel Ltd.*, [1993] 3 S.C.R. 787 ("knowing assistance"), and *Citadel General Assurance Co. v. Lloyds Bank Canada* ("knowing receipt"). Thus, breach of trust actions against a contractor's or subcontractor's bank can arise in circumstances in which the bank has applied trust monies to repay its customer's credit line or otherwise appropriated trust funds on deposit. See *Air Canada v. M & L Travel Ltd.* and cases mentioned in §8.13.

In most cases, wherein a bank, acting in the ordinary course of its business, receives trust monies in good faith, it will not normally be held liable for a breach of trust (*Westex Manufacturing Ltd. v. Wilson* (1986), 21 C.L.R. 133 (B.C.S.C.)). See also *E.B. Horsman & Son Ltd. v. Hongkong Bank of Canada* (1993), 80 B.C.L.R. (2d) 12 (C.A.); *Port Coquitlam Building Supplies Ltd. v. Royal Bank of Canada* (1979), 15 B.C.L.R. 168 (S.C.); *Groves-Raffin Construction Ltd. v. Canadian Imperial Bank of Commerce* (1975), 64 D.L.R. (3d) 78 (B.C.C.A.); *John M.M. Troup Ltd. v. Royal Bank of Canada*, [1962] S.C.R. 487; and *Del Industries Ltd. v. Canadian Imperial Bank of Commerce* (1993), 75 B.C.L.R. (2d) 377 (C.A.).

Applying monies on deposit to a revolving line of credit has been held to be "in the ordinary course of business" of a financial institution (*E.B. Horsman & Son v. Hongkong Bank*). However, where a financial institution knew that its contract or customer was not in compliance with its *Builders Lien Act* responsibilities to its trades, it was found to be in breach of trust for knowingly assisting the general contractor in appropriating trust funds to its general account (*Grinnell Fire Protection Systems Co. v. Bank of Montreal* (1986), 21 C.L.R. 44 (B.C.S.C.)). A bank may be liable if it assisted a trustee in a dishonest or fraudulent design (*Air Canada v. M & L Travel*).

Generally, a bank's liability for breach of trust will turn on its actual or imputed knowledge that trust beneficiaries would go unpaid if the bank appropriated funds on deposit, and evidence of any unusual circumstances that ought to have put the bank on its inquiry. What is, or is not, an "unusual circumstance" will vary on the facts of each case (see *E.B. Horsman and Son Ltd. v. Hongkong Bank*; *Johnson Controls Ltd. v. Avitan Mechanical Installations Ltd.* (1985), 12 C.L.R. 159 (B.C.S.C.); and *Perlmutter Shore Ltd. v. Bank of Montreal* (1981), 34 O.R. (2d) 577 (H.C.)).

If a bank is not shown to have actual knowledge of a breach of trust - for example, trust beneficiaries remaining unpaid - it must be determined whether the bank was aware of facts or circumstances that ought to have put it on its inquiry. The scope of the duty to inquire depends on the nature and length of the relationship between the bank and its customer, the circumstances surrounding the accounts, and whether the case is one of "knowing assistance" or one involving "knowing receipt" of trust property for the bank's own interest (for example, to pay down a customer's overdraft). A lower threshold of knowledge is required to establish a constructive trust arising in circumstances of the

"knowing receipt" of trust monies for the bank's own benefit. In such cases, the bank, as recipient, is held to a higher standard, and knowledge of sufficient facts to put a reasonable person on notice of inquiry as to a possible breach of trust by its customer can attract liability. If a bank fails to make inquiries in these circumstances and is unjustly enriched, it can be required to make restitution (see *Citadel General Assurance Co. v. Lloyds Bank Canada*).

In cases involving "knowing assistance" involving acts in furtherance of a fraud, mere constructive knowledge will not suffice, and a higher standard of actual knowledge, recklessness, or willful blindness will be required to be proven (*Air Canada v. M & L Travel*; see also *Arthur Andersen Inc. v. Toronto Dominion Bank* (1994), 13 C.L.R. (2d) 185 (Ont. C.A.), supplementary reasons (1994), 14 B.L.R. (2d) 1 at 49 (Ont. C.A.), leave to appeal refused (1994), 16 C.L.R. (2d) 233 (note) (S.C.C.)). Banks are imputed with knowledge of the builders lien trust provisions (*John M.M. Troup Ltd. v. Royal Bank*).

It has been held that a bank will not be considered to be vicariously liable for breach of trust, if its inquiry fails to reveal that trust beneficiaries are not being paid. So long as the bank's actions are reasonable, liability will not generally accrue (*Del Industries Ltd. v. Canadian Imperial Bank of Commerce*). Thus, if a bank, acting reasonably, is not aware of circumstances that would indicate that monies were impressed with the trust, it will not generally be guilty of a breach of trust (*Professional Welding Consultants Ltd. v. Bank of Nova Scotia*, [1983] 1 W.W.R. 614 (B.C.S.C.)).

As to cases in which a lender is alleged to be a constructive trustee, and cases of "unjust enrichment", see *Voth Brothers Construction (1974) Ltd. v. National Bank of Canada* (1988), 32 C.L.R. 1 (B.C.C.A.); *Atlas Cabinets & Furniture Ltd. v. National Trust Co.* (1990), 45 B.C.L.R. (2d) 99 (C.A.); *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217; *Citadel General Assurance Co. v. Lloyds Bank Canada*; and *Air Canada v. M & L Travel Ltd.*

#### **E. SUBROGATED TRUST CLAIMS [§8.15]**

Section 10(3) operates to extend the trust rights of beneficiaries by subrogating the rights of a class of beneficiaries to those of the person who engaged that class, in circumstances where the liens of the class of beneficiaries *qua* lien claimants, were discharged by payment under the Act of an amount that is less than the amount owing to the person who engaged the class. Thus, the class of beneficiaries may "step into the shoes" of the person who engaged a class of beneficiaries, and it may seek to exercise that person's rights as a trust beneficiary, against persons higher in the construction pyramid.

**F. LIMITATION PERIODS [§8.16]**

An information charging an offence contrary to s. 11(1) or (3) cannot be laid more than three years after the alleged offence occurred (s. 11(5)) An action by a beneficiary or against a trustee of a statutory trust under the Act must not be commenced later than one year after:

- (1) the head contract is completed, abandoned, or terminated; or
- (2) if the owner did not engage a head contractor, the completion or abandonment of the improvement in respect of which the money over which a trust is claimed became available (s. 14).

The contract is "completed when it is substantially completed or performed"; that is, if the work done under that contract is capable of completion or correction at a cost of not more than:

- (1) 3% of the first \$500,000 of the contract price;
- (2) 2% of the next \$500,000 of the contract price; and
- (3) 1% of the balance of the contract price (s. 1(1) and (2)).

An improvement is "completed" "if the improvement or a substantial part of it is ready for use or is being used for the purpose intended" (s. 1(3)). A contract or improvement is deemed to be "abandoned" on the expiry of a period of 30 days during which no work is being done in connection with the contract or improvement, unless the cause for the cessation of work was and continued to be a strike, lockout, sickness, weather conditions, holidays, a court order, shortage of material, or other similar cause (s. 1(5)).

The trust action is commenced by writ of summons in the Supreme Court and recourse may be had to the Rule 18A procedures under the Supreme Court Rules (*Langley (Township) v. Canada (Revenue Canada Taxation)* (1980), 19 B.C.L.R. 223 (S.C.)). See FP 36 for sample language for use in a trust action statement of claim, and see FP 40 for a sample writ of summons.