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Suppliers' Statutory Trust Under the *Construction Lien Act*

The Ontario Court of Appeal has considered whether, as a means of protecting the contract price of a supplied improvement, a building supplier is entitled to the benefit of a statutorily-established trust fund under the *Construction Lien Act*.

Sunview Doors ("Sunview") manufactured custom-made sliding glass doors, which it supplied to Academy Doors & Windows ("Academy"). In turn, Academy acted as subcontractor and installed those doors in retro-fitted and renovated rental and condominium buildings.

An important element of the narrative is that while Sunview knew that the custom-coloured and custom-sized doors were intended for specific installations by Academy, it never knew the location of the installations, since Academy always picked up the doors at Sunview's manufacturing facility. Neither the orders by Academy nor the invoices from Sunview identified the location of the installations.

When Academy failed to pay Sunview for over $90,000 in doors it had ordered, Sunview attempted to determine the location of the doors, but Academy refused to disclose the information and actively frustrated Sunview's other attempts. Academy went bankrupt shortly after. Ultimately, Sunview sued Academy for breach of contract, and for remedies for breach of trust under the *Construction Lien Act*. Specifically, s. 8(1) of that Act protects the contract or subcontract price of an improvement, and statutorily creates a trust fund for the benefit of "persons who have supplied services or materials to the improvement." Sunview accordingly argued that it was entitled to the protection of s. 8(1) under these circumstances.

At trial, the judge did award Sunview the full amount of its claim, but declined to allow it to benefit from the statutory trust in s. 8(1) of the Act. This is because while Academy was a subcontractor and Sunview was a supplier, Sunview's ignorance of the location of the doors' installation meant it could not satisfy an important requirement: that at the time they were sold or supplied to Academy, Sunview intended that they be used for "known and identified" improvements. This last stipulation stemmed from earlier legal judgments which considered the proper interpretation of the Act, and which the judge felt imposed a threshold test for Sunview's recourse to the statutory trust.

Sunview successfully appealed to the Divisional Court, and Academy appealed further to the Ontario Court of Appeal.

The Court of Appeal concluded that – contrary to the earlier case law on which the trial judge had relied – there was nothing in the wording of s. 8(1) that required that Sunview intend the material be incorporated into a "known and specific improvement" at the time of the sale to Academy. Rather, it was sufficient for the Act's purposes that Sunview was merely able to link the doors to the improvement for which Academy (as subcontractor) was owed money or had been paid. After a careful review of precedent decisions together with consideration of the Act's overall scheme, intent and historical origins, the Court of Appeal could find no authority for the proposition that the Act's wording required Sunview to have intention or knowledge of Academy's *specific* use of the doors at the time it entered into the contract to supply them. The court said:

"Reading in a requirement that the supplier intend that the materials supplied be incorporated into a specific improvement in order for a trust to arise is not consistent with the imposition of a statutory trust."

Therefore, as long as a link "to the improvement" could be established, then Sunview was entitled to the benefit of the s. 8(1) statutory trust.

The Court of Appeal also observed that the purpose of s. 8(1) is to create a statutory trust as a form of security, to ensure suppliers such as Sunview are paid the money they are owed by subcontractors such as Academy. It wrote:

"The object of the Act is to prevent unjust enrichment of those higher up in the construction pyramid by ensuring that money paid for an improvement flows down to those at the bottom."

After concluding that Sunview was eligible to benefit from the statutory trust, the Court went on to find Academy liable not only for breach of contract but for breach of trust under the Act as well.

This was allowed even though Academy had deliberately frustrated Sunview's attempts to get information on where the doors were located and thereby establish the necessary link to the renovations. In these circumstances, the court found that "[p]recedent, principle and policy" dictated that Academy's conduct should not be condoned, and that its unjust enrichment at the expense of Sunview should not be tolerated. As such, the necessary link should be acknowledged in Sunview's favour.

Finally, in light of Academy's bankrupt status, the court found that three individual officers and directors were jointly and severally liable to Sunview for the cost of the doors. See: *Sunview Doors Ltd. v. Academy Doors & Windows Ltd*., 2010 (ONCA).

Trial of Property Appraiser's Liability to Bank Allowed to Proceed

An Ontario Court has allowed for a dispute between a bank and a property appraiser to proceed to trial, in a situation where the fraud of the bank's own lawyer caused it almost $300,000 in losses.

In 2004, the Bank of Montreal was asked to

provide residential mortgage financing to a buyer on certain property being purchased for $360,000. It retained Reliable Appraisal Services to furnish a property appraisal. That appraiser valued the property at $360,000.

Based on that appraisal, the bank agreed to advance 75% of the property's value, *i.e.* $270,000.

The bank's own lawyer advised that he had registered a first mortgage for $270,000 in the bank's favour. In reality, the lawyer acted fraudulently and registered only a second mortgage. This meant that when the mortgage later went into default and the property was sold in 2007 for $347,000 under a power of sale, the bank suffered a total loss, since it held merely a second mortgage rather than a first mortgage.

Realizing that it would be unable to recover from the lawyer who fraudulently certified the second mortgage, the bank sued the appraisers for damages on the basis that they had overvalued the property by $100,000.

Both the bank and the appraiser filed motions for summary judgment, and the court was asked to rule on them. In support of its motion, the bank filed evidence of an expert appraiser to the effect that the property was actually worth $260,000, not $360,000. That expert also gave evidence that if the bank had known of the much lower appraisal (and the unusually-large discrepancy between appraisal and sale values), in all likelihood it would not have proceeded with the decision to advance the funds.

For the purposes of the summary judgment motion, the court assumed that the appraiser was negligent, but still had to determine whether that negligence actually *caused* the bank's $270,000 loss in full. The appraiser countered with the assertion, among other things, that it was the fraudulent lawyer who was the sole cause of the bank's loss: absent the lawyer's fraudulent misdeed, the bank would have had a first mortgage as it expected, and (after the power of sale proceedings) would have been able to recover the full amount of the funds it had advanced.

While the court admitted that it might be a "close call" on the facts, it ultimately accepted the evidence of the bank's expert to the effect that the bank would not have entered into this transaction in the face of a $260,000 appraisal on a property selling for $360,000. Using the well-established legal test, it found the bank would not have advanced funds "but for" the negligent appraisal.

As a result, the appraiser's motion for summary judgment was dismissed, and the matter was allowed to proceed to a full trial. See *Bank of Montreal v. 1576998 Ontario Inc*., (*c.o.b. as Reliable Appraisal Services*, 2010 (ONSC)

Legislative Bar to Oral Mortgage Extensions Confirmed

In the late-2010 decision in *McMurdo v. Saleem*, the court addressed two noteworthy elements of mortgage remedies: 1) it confirmed that oral evidence of a mortgage extension contravenes the *Statute of Frauds*; and 2) it considered its own evidence-assessing powers in connection with summary judgment and the determination of whether there is a "genuine issue for trial."

The facts of the case were straightforward: McMurdo was the mortgagee who held a mortgage on Saleem's home. The principal became due at maturity, but Saleem defaulted on repayment. McMurdo then brought a motion for summary judgment. The main question for the court was whether there had been oral agreement between Saleem and McMurdo to extend the loan, as Saleem claimed.

The court found first of all that no such extension agreement existed, and that there was no genuine issue for trial. It granted summary judgment on the mortgage to McMurdo.

In doing so, the court reflected on its own enhanced judicial powers under the newly-amended Rule 20.01 of the Rules of Civil Procedure. In the context of an application by a party for summary judgment, that Rule allows a court to weigh evidence, assess credibility, and draw reasonable inferences from the evidence, all as part of its role in determining whether there is a "genuine issue for trial."

Using this evidence-assessing power, the court found that Saleem's version of events relating to the alleged oral extension lacked credibility and was inconsistent with other established facts. For example, the parties had previously renewed the mortgage in writing – not orally – which showed that they had knowledge of the correct procedure for agreeing to an extension.

More importantly, the court observed that even assuming McMurdo and Saleem had agreed verbally to extend the loan, this arrangement would be contrary to the *Statute of Frauds* (which requires that all such agreements must be in writing). Such an agreement would also be contrary to the Rules governing court procedure, which provide for certain rules relating to oral evidence, and would offend the express terms of the particular mortgage which prohibited extensions and renewals.

This being the case, Saleem was ordered to repay McMurdo the principal amount of the mortgage together with pre- and post-judgment interest; McMurdo was also awarded possession of the property. See *McMurdo v. Saleem*, 2010 (ONSC)

LEGAL ALERTS

Further Changes for CMHC-Insured Mortgages

On January 17, 2011, the federal government announced additional changes to CMHC-insured mortgages, in addition to those that were introduced in 2010. The changes include measures designed to:

- reduce the maximum amortization period from 35 to 30 years;
- lower the maximum refinancing amount to 85 percent of the value of the home; and
- eliminate CMHC insurance on non-amortizing lines of credit that are secured by homes.

The new changes will come into force on April 18, 2011.

FSCO Changes on Electronic Service and Delivery

The Superintendent of the Financial Services Commission of Ontario (FSCO) has announced the intent to publish a new Electronic Service and Delivery and Filing Rule and a new Mandatory Electronic Filings Rule, both of which will apply to the mortgage brokering industry in 2011.

The Electronic Service and Delivery and Filing Rule formalizes the Superintendent's current practice, which is to serve or deliver notices, statements and other records to mortgage brokers electronically, *i.e.* by way of e-mail.

The Mandatory Electronic Filings Rule replaces the existing Superintendent's Rule – E-filing a Mortgage Brokerage or Administrator Annual Information Return, and requires certain information to be filed by brokers electronically. However, despite the new rule the e-filing of the Annual Information Return submitted by brokers will remain optional.

Ron Fairbloom Joins the Firm

Ron is the newest member of our team of lawyers. His practice involves all aspects of real estate acquisition, condominium/subdivision law, financing, restructuring and sale with a particular emphasis on land development. He has also assisted developers in registering numerous plans of subdivision and plans of condominium in Ontario. He earned his B.A. from York University in 1991, his LLB from Osgoode Hall Law School in 1999 and was called to the Ontario Bar in February 2001.