



Thomas G. Heintzman, O.C., Q.C.

McCarthy Tétrault

Toronto, Ontario

www.mccarthy.ca

416-362-1812

theintzm@mccarthy.ca

www.constructionlawcanada.com

Thomas Heintzman is counsel at McCarthy Tétrault in Toronto. His practice specializes in litigation, arbitration and mediation relating to corporate disputes, shareholder's rights, securities law, broadcasting/telecommunications and class actions.

He has been counsel in many important actions, arbitrations, and appeals before all levels of courts in many Canadian provinces as well as the Supreme Court of Canada.

Thomas Heintzman is the author of Goldsmith & Heintzman on Canadian Building Contracts, 4th Edition which provides an analysis of the law of contracts as it applies to building contracts in Canada.

Goldsmith & Heintzman on Canadian Building Contracts has been cited in 183 judicial decisions including the two leading Supreme Court of Canada decisions on the law of tendering:

M.J.B. Enterprises Ltd. v. Defence Construction (1951), [1999] 1 S.C.R. 619 and
Double N Earthmovers Ltd. v. Edmonton (City), 2007 SCC3, [2007] 1 S.C.R. 116-2007-01-25 Supreme Court of Canada

What Is The Role Of Owners and Contractors In The Application Of Trust Funds?

Construction Law - Construction Liens - Trust Fund Provisions

The Ontario Court of Appeal has recently considered some interesting issues relating to the trust fund provisions of the Construction Lien Act of Ontario. In *Colautti Construction Ltd. v. Ashcroft Development Inc.*, the Court provided some useful guidance about the roles of owners and contractors in the application of trust funds. The Court also held that those provisions cannot be enforced by the owner, but only by the subcontractors or suppliers for whose benefit the provisions were enacted.

Ashcroft was the developer of residential and commercial real estate. Colautti contracted with Ashcroft to provide services in relation to the construction of basements, municipal services and roads under seven different contracts. Colautti also provided services for Ashcroft in relation to the projects under certain older contracts. During the early stages of the projects,

each time Ashcroft paid Colautti, it told Colautti which invoices of Colautti it was paying. But later in the projects, Ashcroft refused to advise which invoices it was paying and for which contacts or projects, even though Colautti made repeated inquiries. Colautti applied some of the monies it received against the oldest contracts. Ashcroft later objected to the application of the funds by Colautti, alleging that Colautti had been paid on the seven contracts that it was suing under, if the payments were applied as Ashcroft maintained they should be.

The court held that Colautti had acted properly in the application of the payments, particularly in the absence of any contemporary advice from Ashcroft about which invoices it was paying. The court applied two principles.

First, a contractor has an obligation to make reasonable inquiries of the debtor, to determine which invoices are being paid by the debtor. The court held that Colautti had fulfilled this obligation.

Second, absent an allocation of a payment by the debtor, the creditor can make the allocation. The court applied the words of the House of Lords in *Cory Brothers & Co. v. Owners of the Turkish Steamship "Mecca"*, [1897] A.C. 286, at p. 293:

“When a debtor is making a payment to his creditor he may appropriate the money as he pleases, and the creditor must apply it accordingly. If the debtor does not make any appropriation at the time when he makes the payment the right of application devolves on the creditor.”

Accordingly, the court held that Colautti acted reasonably in making the application of the funds it received from Ashcroft, in the absence of advice to the contrary from Ashcroft. The court confirmed that the trust fund obligations of the Act did require Colautti to apply the payments it received to the related projects. But having made reasonable inquiries and receiving no advice from the owner about the matter, Colautti was entitled to make the allocation of the payments to the various contracts relating to the projects, including the older contracts.

The court then dealt with Ashcroft’s claim that Colautti had breached the trust fund provisions of the Act. Ashcroft said that, at each time that Colautti received payments, Colautti had obligations to subcontractors under the seven contracts, and it was obliged to pay those subcontractors at that time. Ashcroft claimed a right to have its payments to Colautti re-allocated to those subcontractors, and particularly the subcontractors on the seven projects in question and not the older projects.

The court held that Ashcroft had no standing to enforce the trust fund provisions in this fashion. The court said that only subcontractors and other parties for whose benefit the trust fund provisions had been enacted could enforce those provisions:

“Simply put, standing to complain of a s. 8 breach of trust is limited to those

“who stand in direct privity with the contractor and who are owed amounts by the contractor”The protected class of creditors are those “down the chain” from the trustee of the s. 8(1) trust fund. The Developers, as owners of the Projects, do not come within that class.”

This decision is a welcome clarification of the trust fund provisions. Those provisions are some of the most important parts of the Construction Lien Act. They provide very substantial protection for contractors, subcontractors and suppliers. Clearly the Ontario Court of Appeal was concerned that an owner could effectively undermine those provisions or use them for a purpose for which they were not intended. The court was not prepared to allow an owner to refuse to allocate funds paid by it and then complain later about the contractor’s allocation of them. Nor was it prepared to allow the owner to use the trust fund provisions for its benefit in that re-allocation effort.

Construction Law-Construction Liens-Trust Fund Provisions:

Colautti Construction Ltd. v. Ashcroft Development Inc., 2011 ONCA 359 (CanLII)

Thomas G. Heintzman
www.constructionlawcanada.com

June 19, 2011