Cash is King: Builders' Lien Security and Statutory Trusts under Alberta's Prompt Payment and Construction Lien Act

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A recent Alberta Court of Appeal decision could have a meaningful impact on the way construction industry stakeholders manage cash flow and address security for liens. In *Tempo Alberta Electrical Contractors Co. Ltd. v. Man-Shield (Alta) Construction Inc.* (*Tempo*), the Court of Appeal decided that security paid into court in accordance with Alberta's lien legislation (now, the *Prompt Payment and Construction Lien Act* or PPCLA), to discharge a lien may be substituted, provided there is no prejudice to the lien holder. However, where security is cash and where those funds are, by operation of section 22 of the PPCLA, impressed with a statutory trust after a certificate of substantial performance is issued, a substitution may not be appropriate.

In *Tempo*, The Court of Appeal continued a debate started by the Supreme Court of Canada in *Stuart Olson Dominion Construction Ltd. v. Structal Heavy Steel* (*Structal*) regarding posting security to vacate liens and discharging trust obligations under builders' lien legislation. While this decision provides clarity regarding a party's ability to substitute security under the PPCLA, it demonstrates a possible trend in judicial decision-making when it comes to trust claims in the construction law context that may, in some ways, be creating a security where none expressly exists.

The key takeaways from the decision include:

1. Cash and a lien bond may be substituted provided there is no prejudice to the lien holder.
2. Where cash has been paid into court and trust provisions have been engaged, no such substitution will be allowed.
3. Parties should carefully evaluate the effect of the trust provisions under the PPCLA on the flow of payments through the contractual chain.

Facts

This issue arose in the context of ongoing litigation resulting from the construction of a seniors' care facility in Edmonton. After the subcontractor posted a certificate of substantial performance, the owner paid cash into court to obtain the discharge of the

subcontractor's lien. The owner later settled with the general contractor, assigning the cash paid into court to the general contractor as part of the settlement.

The general contractor applied to replace the security in court with a lien bond. Having been successful at the lower courts, and with no application to stay the applications judge's decision, the general contractor replaced the funds in court with a lien bond prior to the Alberta Court of Appeal's decision. Accordingly, the subcontractor sought the repayment of the cash into court pending a global resolution of the dispute.

Substituting Security or Cash

Posting security into court to discharge builders' liens is a key function of lien legislation. The registration of a lien on title to a project stays the hand of the paymaster, which can bring a project to a halt, expose those continuing to work to increased risk of non-payment, and create cash flow challenges. To mitigate these consequences, the PPCLA creates a process by which the lien may be discharged, the contract funds may continue to flow and the lien claim can be resolved without compromising the protections afforded to the lien claimant.

Where security is posted for the amount of the lien claim, plus costs, the security will stand in place of the land and the registered lien will be discharged from title. It is typical to post a lien bond, rather than cash, as security to discharge a lien in order to maximize operational cash flows. Once the lien has been discharged, the owner can resume making payment in accordance with the PPCLA.

Section 48 of the PPCLA is, however, silent on the ability to replace cash with another form of security (or vice-versa). On that point, the Alberta Court of Appeal concluded that section 48 of the PPCLA permits substitution of the form of security absent demonstrable prejudice to the lienholder.

However, the nature of a lien bond is such that if the lien is ultimately determined to be invalid, the claim against the bond is extinguished. Unlike a lien bond, where cash has been paid into court the funds paid into court may also be impressed with a trust and a breach of trust claim could still be made against the funds even if the lien claim is found to be invalid. Accordingly, because a lien bond would not respond to a breach of trust claim, replacing funds that are impressed with a statutory trust with a lien bond could effectively reduce a claimant's ability to enforce its trust claims. Doing so arguably creates a risk that the funds impressed with a trust may be improperly spent outside the contractual chain.

In *Tempo*, the Alberta Court of Appeal focused on this issue when deciding the lower courts erred and that the application for the substitution of the security ought to have been dismissed. Though each case must be considered on its facts and the specific wording of the applicable lien legislation, similar judicial activism has been exercised in comparable Manitoba cases[1] and is present in the Supreme Court of Canada's reasoning in the *Structal* case.

Conclusion

Notably, section 48 of the PPCLA is directed at providing security for lien claims and not trust claims. In *Tempo, the* cash paid into court by the owner pursuant to section 48 of the PPCLA stood in place of the land and served to discharge a builders' lien, not as security for the subcontractor's trust claim (which had not even been advanced). Nonetheless, the Alberta Court of Appeal determined that the cash paid into court was impressed with a statutory trust and therefore should not be substituted with a lien bond and released to the general contractor. This was despite the fact that the lien claimant would suffer no prejudice to its lien claim, which suggests the Court came to this conclusion based on the prejudice that the substitution of security may have on a statutory breach of trust claim. Consequently, parties dealing with posting security after the trust provisions of the PPCLA have been engaged should carefully evaluate what the best form of security will be to maximize cash flow, while recognizing that payments received from the owner may have restrictions on their use.

If you have any questions related to this article or any other construction related issues, please reach out to one of our construction lawyers.

[1] See for example, *Shawano Consulting Services Ltd. et al. v. Penn-Co Construction Canada (2003) Ltd. et al.*, 2022 MBQB 134 and *Bird Construction Group v. Trotter and Morton Industrial Contracting Inc.*, 2021 MBQB 233.

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