

## Law Reform Notes

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*Law Reform Notes* is produced in the Legislative Services Branch of the Office of the Attorney General. It is distributed to the legal profession in New Brunswick and the law reform community elsewhere, and is available on the Office of the Attorney General's website. The *Notes* provide brief information on some of the law reform projects currently under way within the Branch, and ask for responses to, or information about, items that are still in their formative stages.

We welcome comments from any source. If any of our readers are involved either professionally or otherwise with groups or individuals who may be interested in items discussed in these *Notes*, we encourage them to let them know what the Branch is considering and to suggest that they offer their comments.

Opinions expressed in the *Law Reform Notes* merely represent current thinking within the Legislative Services Branch on the various items mentioned. They should not be taken as representing positions that have been taken by either the Office of the Attorney General or the provincial government. Where the Office or the government has taken a position on a particular item, this will be apparent from the text.

### **1. Enforcement of Money Judgments Act and Debtor Transactions Act**

We have been advised that proclamation of the *Enforcement of Money Judgments Act* and the *Debtor Transactions Act* has been put on hold. When we have information about the timing of proclamation and commencement we will pass it along.

### **2. Powers of attorney legislation**

We continue to work on proposals for powers of attorney legislation. We have received several responses to the items on this topic in the two previous issues of the *Law Reform Notes*, and we remain open to further comments.

The current law in New Brunswick is a combination of common law rules, provisions on powers of attorney for property (sections 56 to 58.7 of the *Property Act*) and provisions on powers of attorney for personal care (sections 40 to 44 of the *Infirm Persons Act*). We plan to propose that these provisions be replaced by a new Act that relates to both types of powers of attorney.

The Act would focus on enduring powers of attorney (EPAs) – those under which the attorney (donee) may exercise his or her authority during the incapacity of the donor, either because the authority continues despite the donor’s loss of capacity or because it commences, or “springs”, when the donor loses capacity. In all likelihood, the Act would provide for the following, among other things:

- execution requirements;
- eligibility requirements for attorneys;
- multiple attorneys;
- commencement of the attorney’s authority;
- duties, powers and limitations of the attorney;
- remuneration of the attorney;
- revocation of an EPA;
- termination of an attorney’s appointment;
- recognition of EPAs from other jurisdictions;
- the status of existing EPAs;
- the relationship between EPAs and health care directives.

We are in the process of considering how the Act should deal with these and other matters. Below is a discussion of some of the issues that have come up in our review of the law reform literature, legislation in other jurisdictions, case law, and responses we have received. We welcome comments on these issues or any other aspect of this area of law.

### **Protection of donors**

In recent years, a number of law reform agencies and other groups have recommended that measures be added to powers of attorney legislation to protect donors from financial abuse.

One such measure is the exclusion of certain classes of persons from acting as an attorney: those who have been convicted of specified offences (theft, fraud etc.), those who provide paid personal care or health care services to the donor, and undischarged bankrupts. The legislation in some jurisdictions contains such exclusions. It seems to us that this could prevent some donors from appointing an unsuitable attorney. On the other hand, it could limit donors’ options, which in some cases are already limited, and could increase the number of invalid EPAs and complicate the task of determining whether an EPA is valid.

Another measure is a notice requirement. The EPA would name a person or persons who are to receive notice – family members or close friends, for example – and the attorney would be required to give notice to those persons before acting under the EPA. The notice would describe the attorney’s duties and the options available in the event of suspected abuse. It has been recommended that this notice requirement be mandatory for all attorneys, and that if the EPA does not name a person to receive notice, the attorney would be required to give notice to the donor’s immediate family members (spouse or partner, siblings, adult children, parents).

We think that some form of notice by the attorney would likely be beneficial. It could reduce both innocent misuse and intentional abuse of EPAs by informing the attorney and others of what is involved and what

to do if concerns arise. However, we think that notice should probably not be mandatory for all attorneys. The donor should be able to choose whether the attorney is required to give notice and, if so, to whom. A donor may prefer to keep his or her affairs private and may have good reasons not to share information with all immediate family members.

A related measure is the appointment of a monitor – a person who is entitled to demand an accounting from the attorney. Some jurisdictions provide for this, and also provide that if no monitor is appointed a family member may demand an accounting. We think that providing for such an appointment is probably sensible, but that the lack of an appointment should not entitle family members to demand an accounting. Again, the donor should be able to choose.

We are also considering the possibility of a reporting and investigation process. At present, when abuse of an EPA is suspected the options are limited. The main remedies – an application to the court for an accounting or for the appointment of a committee, and a report to the police – would be undesirable or ineffective in many cases. Several provinces have a process through which suspected abuse can be reported to a public body and investigated. We are in the process of exploring options.

### **Standard form**

Our review has also led us to consider whether an optional standard form EPA should be developed. Other jurisdictions have an optional form (Prince Edward Island), explanatory materials (Yukon, Manitoba) or both (British Columbia, Saskatchewan, Ontario, Northwest Territories). (Quebec has a guide and optional form for “protection mandates”, which are analogous to EPAs.) These forms allow people to prepare an EPA without legal advice. They guide users through the various options and requirements using plain-language instructions and information.

If an optional standard form were to be developed, it would probably make sense not to retain the sealing requirement. At present, the *Infirm Persons Act* requires that powers of attorney for personal care be made under seal (s. 40(1)), and it is our understanding that sealing is the norm for powers of attorney for property, due to common law rules and to the fact that the two types of power of attorney are often combined in a single document. A sealing requirement would be an obstacle for those who wish to prepare an EPA without legal advice, which would undermine the purpose of the standard form. No other jurisdiction in Canada has a sealing requirement, and only one requires the involvement of a lawyer (Yukon).

The main benefit of a standard form would be accessibility. New Brunswickers for whom access to legal services is difficult, for financial or other reasons, would be able to prepare an EPA and enjoy the attendant benefits. This would not ensure that everyone has an EPA – even in jurisdictions with standard forms many people do not have one – but it would likely increase their prevalence.

A potential drawback is that people who would otherwise obtain legal advice will not do so, and will therefore be more likely to create an EPA that is invalid or insufficient or a product of undue influence. It is not clear to us, though, whether a standard form would result in fewer people obtaining legal advice, especially given that an EPA is often prepared when a client is in the lawyer’s office to have a will prepared.

### **Financial institutions**

We have received comments expressing concern about certain practices of financial institutions. Apparently, donors are sometimes asked to use the financial institution’s own EPA template. This may discourage donors from creating an EPA that reflects their needs, and may have the effect of revoking a

previous EPA. Also, we have heard that financial institutions sometimes refuse to recognize the validity of a (non-springing) EPA unless the donor confirms, in person, that the attorney is authorized or the attorney provides a letter from a physician stating that the donor is incompetent. This may cause hardship for some and is at odds with the purpose of an EPA.

On the other hand, we have also received comments describing concerns that financial institutions and other third parties have about their role in identifying and reporting abuse of EPAs. There is uncertainty as to what the limitations of an attorney are, what to do when abuse is suspected, and whether privacy legislation prevents them from reporting.

Some of these concerns may be addressed by the provisions mentioned above on the limitations of an attorney, the commencement of an attorney's authority, and a reporting and investigation process. We are considering whether it would also be helpful to include provisions regarding the recognition of EPAs by third parties.

### **Powers of attorney and health care directives**

As discussed in *Law Reform Notes #39*, the *Advanced Health Care Directives Act* (AHCDA) added "health care directives" and "proxies" to the landscape. Health care directives overlap with powers of attorney because both an attorney for personal care and a proxy can make health care decisions, and because both a power of attorney for personal care and a health care directive can contain directions regarding health care. The AHCDA contains provisions that address the relationship between these two types of document, but the overlap remains.

We are considering how the new Act should deal with this. There are a few options. First, the Act could retain the overlap – by providing that powers of attorney for personal care can relate to health care – and address how conflicts with health care directives are to be resolved. Second, the Act could remove the overlap by providing that powers of attorney for personal care are limited to matters that are outside the scope of the AHCDA – i.e. personal care decisions that do not relate to health care. (Saskatchewan has taken this approach.) Third, the Act could remove the overlap by incorporating the provisions of the AHCDA into the new powers of attorney Act. This option may not be viable, for practical reasons, but at this stage we are considering all of the options.

### **3. Mechanics' Lien Act**

The *Mechanics' Lien Act* (the "Act"), like most Canadian construction lien legislation, has long been the subject of criticism and, in our view, is long overdue for reform. The common sentiment is that construction lien legislation is cumbersome, hard to understand, costly to apply, and often of limited help to those it was most intended to protect – suppliers of labour, services and materials at the bottom of the construction pyramid. Most recently, the Act has been criticized for failing to address the issue of payment delay, a critical issue in today's construction industry.

In light of these criticisms, we have taken on the project of reforming the Act. We note at the outset that reform in this area has historically been difficult, given the large number of stakeholders and their varied and often conflicting interests. We are nevertheless hopeful that the present effort will result in practical, positive change for the New Brunswick construction industry.

Given the size of the task at hand, we are dividing our discussion over two issues of the *Law Reform Notes*. In this issue, we address the modernization of the existing legislation. In the next issue, which we anticipate publishing in early 2018, we will address the issue of prompt payment, including the

adjudication of payment-related disputes. We offer a brief overview of the latter topic, along with references to key resources, at the end of the present discussion.

The list of issues and potential changes set out below is lengthy, but non-exclusive – we invite readers to raise any other issues that might be of concern. We ask that comments on this issue of the *Law Reform Notes* be submitted by February 15, 2018. There will be a second comment period after the release of the next issue.

### **Modernizing the existing legislation**

We begin by stating that we do not anticipate making any major changes to the core elements of the Act: in general, liens, holdbacks and construction trusts will continue in their present form. We do, however, plan to make a number of changes and additions intended to improve the functioning of these mechanisms and to address specific concerns raised by stakeholders. We also intend to update the language and style of the Act to reflect modern drafting conventions. We suspect that this, in and of itself, will make the Act more useful. The end result will likely be a new Act, tentatively titled the *Construction Act*.

In developing the questions and suggestions below, we have considered commentary (academic and practitioner), case law, comments sent to us, and prior law reform efforts. We have paid particular attention to the final report of the Expert Review of Ontario’s *Construction Lien Act* (the Expert Review), released in April 2016. This report was the product of a 14-month review conducted by experts Bruce Reynolds and Sharon Vogel, at the request of the Ontario government. The core issues of their mandate were modernization of the Act, promptness of payment and the effectiveness of dispute resolution. The mandate also included conducting broad-based consultation within the Ontario construction industry.

The Expert Review ultimately made 100 recommendations aimed at strengthening the Act and allowing it to better achieve its policy objectives. The Ontario government accepted nearly all of these recommendations and has recently passed extensive [amendments](#) to the Act (renamed the “*Construction Act*”). The housekeeping and non-substantive amendments came into force on December 12, 2017; the more substantive amendments will be phased in gradually.

While there are differences between the New Brunswick and Ontario legislation and industry practices, they are similar enough that many of the Ontario proposals could, with some adaptation, be adopted here. The report and supporting documents (e.g. stakeholder submissions) are available on the Expert Review’s [web site](#).

#### Definitions (s. 1)

We are considering broadening the definitions of “improvement” and “owner”.

“Improvement” is currently defined as including “anything constructed, erected, built, placed, dug or drilled on or in land except a thing that is not attached to the realty nor intended to be or become part thereof” (s. 1).

We are considering expanding this to include the installation of equipment (e.g. industrial, mechanical or electrical) that is essential to the normal or intended use of the lands or building. This would address cases such as *Beloit Canada Ltd. v. Fundy Forest Industries Ltd.* (1981), 37 NBR (2d) 17, [1981] N.B.J. No. 280 (QL) (CA), in which a large machine installed in a pulp mill was found *not* to be an “improvement”, because it was still capable of being moved. Similar changes were made in Ontario in 2010 after the decision in *Kennedy Electric Ltd. v. Dana Canada Corporation*, 2007 ONCA 664, [2007]

O.J. No. 3657 (QL), after the addition of an assembly line to a vehicle manufacturing plant was found to not be lienable.

We are also considering expanding the definition of “owner”. Over time, the concept of ownership has become more complex as projects have increased in complexity and as new types of contractual arrangements have developed (e.g. public-private-partnerships, “P3s”). The current definition of “owner” does not account for these complexities and, in Ontario at least, stakeholders have complained that this has led lien claimants, unsure of who the “owner” actually is, to “lien everyone”. The Expert Review recommended that the definition of “owner” be amended to provide for multiple owners on such projects, such that special purpose vehicles (“Project Co.”) are included as owners and it is “Project Co.” that is responsible to maintain holdbacks.

We suspect there are likely similar difficulties with respect to these kinds of projects in New Brunswick.

### Liens

#### *Minimum amount of lien claim (s. 4(4))*

The minimum lien claim is currently set at \$100. This has not changed since 1965 and is inordinately low given the effects of inflation (\$100 in 1965 dollars equals approximately \$772 now). It is our view that this limit should be raised (likely to \$1000) and should, in future, be prescribed by regulation to facilitate more frequent increases. While this would cut off access to the lien remedy for small value claims, it is our sense that the number of such claims that are actually pursued is likely very small. Such claimants would still have the right to bring a small claim.

#### *Time period for preservation (s. 24)*

Section 24 of the Act provides that a claim of lien for services or wages must be filed within 30 days from the completion of services or the last day of work, while a claim of lien for materials must be filed within 60 days from the furnishing of last material. Only the three Maritime provinces continue to use two different preservation periods. In 1993, the CBA (NB) special committee on reform of the Act recommended that this distinction be eliminated and that a single time period of 60 days be established. We tend to agree.

#### *Termination as a triggering event (s. 24)*

Section 24 of the Act contains two “triggers” for the commencement of the preservation period – completion or abandonment. Based on stakeholder feedback in Ontario, the Expert Review recommended that “termination” also be added as a trigger. This would account for situations in which one of the parties repudiates the contract. The Expert Review noted that this would help fill a “possible gap” and provide added clarity. British Columbia’s legislation currently includes “termination” as a triggering event. We think “termination” should also be included as a trigger here.

#### *Vacating liens by posting of security (s. 51)*

Section 51 of the Act allows a party to vacate a lien from title pending disposition of a dispute by paying security into court. This can take the form of cash or other equivalent security (certified funds, lien bond, letter of credit). Two concerns have been raised in respect of the posting of security:

- *Amount of security* – The process of determining how much security should be posted can be time-consuming and expensive, possibly requiring multiple court hearings. Determining an appropriate amount is particularly difficult on large projects where there may be multiple, overlapping claims of lien.

- *Acceptable forms of security* – In Ontario, some stakeholders expressed the concern that courts were being presented with, and accepting, lien bonds that were not from recognized sureties and, in some cases, from individuals without bonding capacity and of unknown financial status.

We have heard that the first is a problem in New Brunswick and suspect that the second may be as well. In Ontario, the first issue has been addressed, at least in part, through the use of lien bonds. The second issue has been addressed through legislation prescribing in some detail what forms of security are permissible.

*Liens against specific kinds of property – subdivisions, condominiums and leaseholds*

Stakeholders in Ontario expressed concerns that the process of preserving and enforcing liens was becoming increasingly difficult with respect to certain kinds of property, including condominiums (e.g. lien on common areas), residential subdivisions, and leasehold interests (e.g. landlords who use “creative” means to artificially shield themselves from liens). Though some of the relevant law differs between New Brunswick and Ontario, we suspect that similar problems may exist here. We are open to making recommendations in this area, but before doing so need a clearer picture of what problems have arisen in New Brunswick.

*Abuse of lien rights*

The New Brunswick Act does not specifically address abusive, frivolous, vexatious, exaggerated, false, expired, or nuisance lien claims, though s. 51(2) allows a judge to order the filing of a claim of lien to be vacated “upon any ... proper ground”. The only other provision that touches on the topic is section 57, which provides for costs consequences where a party does not take the “least expensive course”.

Other jurisdictions have chosen to address abusive lien claims more directly. Ontario, for example, gives a specific right of action for damages caused by a person who preserves a claim for lien or gives written notice of lien where the person knows: (a) the amount is grossly exaggerated, or (b) he or she does not in fact have a lien (s. 35). The Ontario Act also provides for a specific right to cross-examine on the affidavit of the lien claimant, without an order, regardless of whether an action has been commenced, which is seen as another way of guarding against invalid or inflated liens (s. 40).

We see the benefit of the Ontario approach and are considering recommending it. Before doing so, however, we would like to have a better idea of the scope of this problem in New Brunswick and whether there might, from the perspective of those in the industry, be better ways of dealing with it.

*Preliminary notice to owners*

We are also considering whether those who supply services or materials to an improvement should be required to provide owners with: (a) notice they are contributing to the improvement, and (b) advance notice of their intent to file a claim of lien. Such notices are intended to address the problem of the “uninformed householder”, though improved notice requirements might be of benefit to owners more generally.

The “uninformed householder” issue involves two related problems. The first is the risk of “double payment” caused when a homeowner pays the builder in full, without retaining a holdback (because he or she lacks awareness of the Act or disregards it). If the builder then fails to pay its subcontractors or suppliers, they place liens, and the homeowner will be called upon to pay again to have those liens removed. The second problem is “secret liens”, in which a lien is placed by a subcontractor or supplier that the homeowner did not even know was contributing to the improvement.

Several American states have addressed these issues by requiring those who provide services and materials to improvements to give certain “preliminary” notices to homeowners. Based on these schemes, we are considering recommending two notices:

- First, requiring those who supply services or materials, *and* who do not have a contract with the owner, to provide the owner with written notice they are contributing to the improvement, either upon commencing work/supply or within a specified period of time thereafter (e.g. 30 days). The notice, which would likely be set out in a brief, plain- language statutory form, would also advise the owner of his or her rights and responsibilities under the Act (e.g. the need to retain a holdback), and that, in the event of non-payment, their property may be subject to a lien.
- Second, requiring that a lien claimant also provide the owner with advance (e.g. 10 days) written notice of their intent to file a claim of lien. The intent would be to give the owner a reasonable amount of time to try to resolve the payment issue before title was clouded.

To encourage compliance, access to the lien remedy would be contingent on satisfying these notice requirements.

#### *Holdbacks and substantial performance*

##### *Reducing the holdback to 10% (s. 15)*

New Brunswick (along with Prince Edward Island) currently has the highest holdbacks in Canada: 20% when the value of the work and material is \$15,000 or less, and 15% when the value exceeds \$15,000. Most other provinces’ holdbacks are set at 10%; Manitoba’s is the lowest, at 7.5%.

It seems to us that New Brunswick should also move to a single holdback, set at 10%. This is simpler, is in line with other jurisdictions and should enhance the flow of funds down the construction pyramid while still leaving a reasonably sized fund out of which to satisfy liens.

##### *Defining substantial performance*

It has been brought to our attention that imprecision in the term “substantial performance” is causing some issues – determining when this point has been reached can be difficult, sometimes requiring resolution by the courts, possibly years after the fact.

We are considering whether this situation would be improved by specifically defining “substantial performance”, as is done in some other provinces, including Ontario, Manitoba, Newfoundland and Labrador and Nova Scotia. The legislation in these provinces provides that a contract (and a subcontract, in Manitoba) is deemed to be “substantially performed” when:

- (a) the work or a substantial part thereof is ready for use, or being used for the purpose intended;  
and
- (b) the work remaining to be done is capable of completion or correction at a cost of less than a certain percentage of the contract price (the provision sets out a formula).

We see the benefit of including such a definition, but also note that such changes have not put an end to litigation relating to substantial performance in other provinces. In Ontario, one commentator noted that such litigation has nevertheless flourished.

### *Requiring notice of substantial performance/completion*

A second issue relating to substantial performance is that it can be difficult for those further down the construction pyramid to find out when this point is reached and the countdown to holdback release begins. The Act now requires that certain information be provided to contractors, but this does not include disclosure or public notice of substantial performance (s. 32).

We are considering adding a requirement to give notice of substantial performance, similar to the requirements in Alberta, Nova Scotia and Ontario. We find the scheme recently implemented in Nova Scotia to be particularly promising. There, owners are required by [regulation](#) to post a notice of substantial performance of a contract (and notice of completion of a subcontract) both at the job site and on a publicly available [online registry](#) maintained by the Construction Association of Nova Scotia. Single-family residential construction valued at less than \$75,000 is excluded from these requirements.

### *Facilitating early release of holdback (s. 15)*

Another concern we wish to address is the potentially very long wait for holdback release faced by those who provide services or materials early in the life of a project. At present, the Act (s. 15(4)) allows for early release of holdback in some circumstances, but we suspect that these provisions may not be effective in practice. The commentary suggests that in some jurisdictions with similar provisions, owners are nevertheless reluctant to release holdback funds to early subcontractors and suppliers on the grounds that they remain at risk of liens by later subcontractors and suppliers. Owners reportedly prefer to withhold all holdback funds until the principal contract is complete.

We are considering how section 15 might be adjusted to better facilitate the early release of holdback, including:

- where there is no architect, engineer, or other person upon whose certificate payment is made, allowing *the owner and the head/general contractor* to certify that a sub-contract is substantially performed/complete;
- where certification is refused, allowing a subcontractor or contractor to apply to the court for a declaration of substantial performance/completion;
- clarifying that owners are protected from later lien claims and that early holdback release applies to both the main contract and subcontracts.

### *Annual, phased and segmented release of holdback*

The wait for holdback release can also be long on large, multi-year projects and those carried out in phases. At present, the New Brunswick Act makes no provision for early release of holdback in these circumstances. This contrasts with legislation in Manitoba, Saskatchewan, Prince Edward Island and Newfoundland and Labrador, which allow (to varying degrees) for partial, annual release of holdback on some multi-year construction projects. The Ontario Expert Review also recommended that the Ontario legislation be amended to: (a) permit partial release of holdback on either a phased or annual basis, if provided for in the construction contract between the parties, and (b) allow for the segmentation of holdback for projects involving clearly separable improvements, particularly for what are known there as “Alternative Financing and Procurement” projects (e.g. P3s).

Would it be desirable to allow for annual, phased and/or segmented release of holdback in some circumstances in New Brunswick?

### *Mandatory release of holdback (s. 17)*

At present, section 17, which governs release of holdback upon the expiration of the lien period, is permissive (“payments ... may be made”). In the Ontario Expert Review, contractors asked that holdback release under a similar provision be made mandatory. They complained that owners were retaining holdback funds until after their status as holdback funds expired and then setting off against those funds any debts or claims they had against the contractor, whether related to the project or not (i.e. owners were essentially retaining the holdback funds as a deficiency holdback.) The Ontario Expert Review recommended making ordinary (but not early) release of holdback mandatory.

It is not clear to us whether this is also a concern in New Brunswick. If it is, our view is that it would be reasonable to make it clear that release of holdback is *not* optional.

### *Construction trusts*

#### *Clarifying the trust provisions*

Section 3 describes the construction trust in very broad terms, which has led to criticism that it is too vague. Over time, the scope of the trust provisions has been clarified by the courts, but it may be that industry would benefit from having more specificity in the Act, particularly with respect to the duties of a trustee. The Ontario Act, for example, sets out specifically when a payment by the trustee discharges the trust, when the trust funds may be reduced (i.e. when the trustee may retain funds for itself), and when a trustee that has borrowed money for the purpose of the improvement may use the trust funds to discharge the loan.

We would appreciate feedback on whether the common law in this area is sufficient, or whether legislative provisions would be helpful.

#### *Owner's and vendor's trusts*

The New Brunswick Act currently imposes a trust only at the level of the “builder or contractor or a sub-contractor” for the benefit of those who have supplied services or materials to the improvement for the benefit of that builder, contractor or subcontractor. Other provinces have chosen to also impose a trust on certain funds in the hands of owners (Ontario, Manitoba, Saskatchewan) and/or vendors (aimed at owners who sell their interest to avoid a trust claim) (Nova Scotia, Ontario, Saskatchewan).

Including owner's and vendor's trusts would have the advantage of increasing protection for those further down the construction pyramid, but could also create administrative burdens/difficulties. For example, where a project is self-financed by an owner, it can be difficult to know at what point the trust attaches and to which funds. That said, it does not appear that such trusts have created undue hardship on owners or vendors in the jurisdictions that have them.

Would it be beneficial to include owner's and/or vendor's trusts in the New Brunswick Act? There is at least one case in which a subcontractor would have benefited from such a provision (*M. Robert Birmingham Ltd. v. Perth-Andover* (1981), 38 N.B.R. (2d) 14, aff'd 38 N.B.R. (2d) 14 (CA)).

#### *Protecting funds in the event of insolvency*

One of the problems relating to construction trusts is uncertainty in the event of payor insolvency. A specific example is the interaction between section 3 of the Act and section 67 of the *Bankruptcy and Insolvency Act* (property of the bankrupt). The key question has been whether a statutory trust is a “trust” for the purposes of paragraph 67(1)(a), which protects “property held by the bankrupt in trust for any other person” from creditors. Courts have found that the answer to this question is “yes”, provided the trust

meets the common law “three certainties” test. In the context of construction trusts, the issue has been whether there is certainty of subject matter when construction “trust” funds have been co-mingled with other funds.

At present, the Act does not impose an obligation on trustees to segregate funds into separate trust accounts. The result is that, in practice, some trustees co-mingle trust funds with non-trust funds, or with mix funds held in trust for different projects, in one bank account. This puts construction trust funds at risk in the event of insolvency, unless the court is able to make a determination that the funds are traceable, which is not always the case.

In our view, this state of affairs is unsatisfactory, and we are considering whether to increase the protection of trust beneficiaries in the event of insolvency. The Ontario Expert Review considered three potential solutions to this problem: segregated holdback funds, enhanced record-keeping requirements, and project bank accounts. Ontario has adopted the second option. It seems to us that either of the first two options may work for New Brunswick.

In the segregated holdback fund model, when a contractor’s invoice is paid, 90% (presuming a 10% holdback) is remitted directly to the contractor, and the remaining 10% is deposited into a segregated holdback trust account. The details of how such funds are handled vary, but if such a scheme were adopted in New Brunswick, we envision the following key features:

- The owner would establish a separate holdback account, in the joint names of the owner and one other trustee, for each project (as opposed to each contract within a project), into which all holdback amounts would be paid.
- The other trustee would be the contractor, a lawyer, an architect or engineer (who is not the payment certifier), an accountant, a person with experience in the construction industry, or a trust or loan corporation.
- Unless the parties agreed otherwise, interest would accrue to the owner during the holdback period, and to the credit of the contractor from whom the holdback was retained after the expiration of lien rights.
- Where the account contains funds related to multiple contracts, the trustee would be required to follow specific record-keeping requirements to maintain traceability.
- For payment, the signatures of both trustees would be required unless otherwise ordered.
- Trustees would be able to apply to the court for directions as necessary.

Such funds are presently in use in British Columbia (for projects valued at over \$100,000), Manitoba and Saskatchewan (both for projects over \$200,000). Ontario considered and rejected segregated holdback funds in 1983 and again during the Expert Review, though the concept received support from several key stakeholders.

The Expert Review recommended instead the adoption of a system of enhanced record-keeping requirements. This system, more popularly known as “the New York Model”, is based on the [New York Lien Law](#). This law creates a statutory construction trust that is broadly similar to Canadian construction trusts. Funds that are received by owners, contractors and subcontractors, for or in connection with an improvement to real property, are subject to a trust for the benefit of contractors, subcontractors and suppliers. The funds received in connection with each improvement constitute a separate trust. Trustees have the same basic fiduciary duties and loyalties as a trustee of any trust, including: keeping and

rendering accounts, keeping trust funds separate from their own, furnishing information and permitting beneficiaries to examine trust accounts, and enforcing claims on behalf of the trust.

The New York Lien Law also includes a set of standard bookkeeping practices that, if followed, are a *prima facie* defence to a claim of breach of trust. At the recommendation of the Ontario Expert Review, the Ontario legislation is being amended to include similar rules, which will provide that:

- All trust funds are deposited in the trustee's name (i.e. as trustee).
- The trustee is *not* required to keep the funds for each trust in separate bank accounts, provided the trustee's books and records of account clearly allocate the funds deposited in the general account to each individual trust.
- The trustee must keep separate books for each trust and, if funds of separate trusts are in the same bank account, the trustee must keep a record of such account showing the allocation to each trust of deposits and withdrawals.
- The books and records of each trust must show certain particulars with respect to assets receivable, assets payable, trust funds received, trust payments made with trust assets, and any transfers made for the purpose of the trust.

The Expert Review cited two reasons for preferring this model over the segregated holdback fund model: first, the potential administrative burden of maintaining a segregated holdback account, and second, in jurisdictions where segregated holdback accounts are required, some owners simply decline to establish such accounts, as enforcement is apparently limited.

The third option is the project bank account model. In this model, all payees in the construction pyramid are paid from a single project trust account, at the same time. In other words, there is no need to wait for payments to "trickle down" through the construction pyramid. The Ontario Expert review recommended a two-year pilot project that would trial project bank accounts in the public sector, but the Ontario government has indicated it does not intend to propose legislation in this area.

In our view, construction trusts in New Brunswick should be more clearly protected in the event of insolvency. What is less clear is whether segregated holdback funds or the "New York Model" would be a better fit. Both seem to have the potential to create some administrative burden, and both carry a risk of non-compliance. We also have some concern that the latter approach has yet to be considered by a Canadian court, and so there is no guarantee such record-keeping requirements would meet the "certainty of subject matter" test. That determination would likely rest on the quality of the record keeping, which would leave trust funds at continued risk.

### Simplified dispute resolution

#### *Small and intermediate lien claims*

Any proceeding for relief pursuant to the provisions of the *Mechanics' Lien Act* must be heard in the Court of Queen's Bench, a process that can be expensive, time-consuming and complex. This is at odds with the original intent of lien legislation, which was, at least in part, to provide a means of efficient dispute resolution. In practice, the evidence suggests that for relatively small value claims, it is simply not worth the time or money to pursue an action. In Ontario, for example, contractors report that the median cost of pursuing a lien action is \$15,000, and that, for claims below \$25,000, the cost of the litigation process outweighs the benefits of liening. Such claims are also seen as a poor use of the Court's time. We suspect the situation is similar in New Brunswick.

One potential solution to this problem is to move to a tiered dispute resolution process for claims arising under the Act. In short, claims below the small claims threshold (currently \$12,500) could be referred to Small Claims Court and heard according to its ordinary procedure. The referral process is necessary due to constitutional issues – final jurisdiction over lien matters rests with Superior Courts (“Section 96” courts). Larger claims (e.g. between \$12,500 and \$75,000) would still be heard by the Court of Queen’s Bench, but could proceed according to a simplified procedure, analogous (to the extent possible) to Rule 79.

Both the Law Reform Commission of Nova Scotia and the Ontario Expert Review recommended a tiered dispute resolution process for claims arising under lien legislation, though only Ontario has chosen to implement it. In Nova Scotia, it was recommended that both lien and trust claims under \$25,000 be eligible for reference to Small Claims Court. In Ontario, the Expert Review recommended that lien claims of less than \$25,000 be referred to Small Claims Court and that claims between \$25,000 and \$100,000 proceed according to a simplified procedure with limited examinations for discovery and a summary trial procedure. At present, lien claims in Ontario may be referred to specialized lien masters.

We refer readers with a particular interest in this issue to the following reports:

- Law Reform Commission of Nova Scotia  
[Builders’ Lien Act \(Final Report, March 2013\)](#), at 14  
[Builders’ Liens in Nova Scotia: Reform of the Mechanics’ Lien Act \(Final Report, June 2003\)](#), at 27
- Ontario Expert Review  
[Striking the Balance: Expert Review of Ontario’s Construction Lien Act \(Final Report, April 2016\)](#), at 107

The Law Reform Commission of Nova Scotia’s 2013 report is particularly helpful. It considers, at length, a number of topics that would also be relevant in New Brunswick, including what issues should be eligible for reference (validity of a lien, liability in tort and contract, determination of amounts owing, allocation of holdback funds), detailed matters of procedure, capacity of Small Claims Courts (with respect to volume of claims and specialized expertise), the constitutional issue, and lien action references in other jurisdictions.

#### *Arbitration*

Another issue that has been brought to our attention is the relationship between lien legislation and arbitration. More specifically, there is a lack of clarity with respect to the interaction of the Act and section 7 of the *Arbitration Act*, which provides for a stay of proceedings in the event a party to an arbitration agreement commences a proceeding in respect of a matter that is to be submitted to arbitration. Such stays are problematic in the context of mechanics’ liens because of the strict timelines imposed by the Act.

In Nova Scotia, this issue was addressed by adding to that province’s legislation three provisions from the ULCC [Model Liens and Arbitration Provisions 2000](#), which clarify that:

- Lien claimants may take all steps necessary under the Act in order to preserve a lien or the security to which it attaches.

- Any step taken to preserve a lien or security will not be treated as a waiver of the right to arbitrate.
- The effect of a stay pending arbitration is limited to the parties to the arbitration agreement and does not affect third party actions.

We plan to propose that the ULCC provisions, or something similar, be included in the new Act.

#### Right to information (s. 32)

The New Brunswick Act, like those in most other provinces, provides lienholders with a right to certain information from owners, mortgagees, unpaid vendors (or their agents), contractors and subcontractors. The trend in other jurisdictions has been to expand such disclosure rights, and most now impose more extensive disclosure obligations than does New Brunswick.

Even in Ontario, which other provinces have often used as a model for disclosure obligations, some stakeholders have complained that they do not have enough information to make an informed assessment of the risk of non-payment or delayed payment. During the Expert Review, they called for the disclosure of payment schedules, notification of receipt of funds, and financial capability disclosure. The panel declined to adopt these suggestions, but did recommend clarifying what constitutes a “state of accounts” and requiring the release of certain information relating to leaseholds.

In our view, the New Brunswick Act is outdated, and the list of information that must be disclosed should be expanded. The changes we are considering include:

- expanding the list of parties who may demand information to include trust beneficiaries and mortgagees;
- expanding the information that can be demanded of owners, contractors and subcontractors to include the names of parties to the contract, the contract price and a copy of any labour and material payment bond;
- if segregated holdback funds are adopted, requiring owners to provide information related to that account;
- expanding the information that can be demanded of landlords whose interest is subject to a lien.

We are also considering clarifying the term “state of accounts”, setting a time limit for responding to a request for information (e.g. 21 days), and allowing a party seeking information to apply for a court order if the person of whom the demand is made fails to comply.

These suggestions are in line with legislation in other jurisdictions.

#### Bonds

We have been advised that the present Act is also problematic because it fails to recognize or account for the protection afforded by labour and material payment bonds (“payment bonds”). We understand this to mean that the holdback and lien system is redundant when a payment bond is in place. Presuming this is correct, one obvious solution is to allow parties to opt out of the holdback and lien scheme, in whole or in part (i.e. a reduced holdback), if an appropriate payment bond is in place.

This issue was considered in detail by the Law Reform Commission of British Columbia in 1972 (See the Commission’s [final report](#), starting at page 70). It envisioned a system in which the parties at each level in

the construction pyramid would have the option of obtaining a payment bond or of having the person with whom they had contracted retain a holdback. Where a contractor obtained a bond, but its subcontractor did not, the persons employed directly by the contractor would look to the bond for security. Those employed by the subcontractor, however, would look to the holdback retained by the contractor from the subcontractor.

Conceptually, we understand the attraction of such a scheme. In practice, however, it seems to have the potential to be confusing and/or administratively burdensome, especially on larger projects with multiple tiers, in which the terms of the various bonds may not be consistent.

We also highlight the following considerations/concerns:

- The protections offered by payment bonds and the lien and holdback scheme are not necessarily coextensive – it would be important to ensure that claimants under one scheme were not disadvantaged relative to those under the other.
- Before a surety agrees to pay, it is entitled to conduct its own investigation and ensure that its specific contractual terms (which will vary between contracts) have been met. It is also entitled to plead any defence the principal would have to avoid payment of a claim, including relying on “pay when paid” clauses.
- Potential claimants may not be aware a payment bond is in place, let alone its terms.
- Payment bonds in the private sector generally benefit only the first tier of contractors. Whether a bond would respond to claims brought by sub-subcontractors, and what amounts they might claim, would depend on the specific wording of the bond. (We note that the Surety Association of Canada advised the Expert Review that it supports reducing the holdback amount when a payment bond is in place. Further, it is prepared to consider expanding the definition of “claimant” in standard payment bonds to include those past the first tier. It has also pledged to keep working with other key stakeholders and the Expert Review to adjust its products and processes to “arrive at responsive solutions that will benefit all parties”.)
- Some see bonding as too complicated and/or too expensive and, at present, labour and material payment bonds cannot be acquired separately from performance bonds.

Finally, we express some concern that we would be the first Canadian jurisdiction to adopt an “opt out” regime. We are not opposed to being first on principle, but are wary of the risks of doing so, particularly when we are already considering introducing other potentially significant changes.

We welcome comment on this issue, including other suggestions for how payment bonds might be accommodated. We are also interested in comments related to other kinds of bonds and whether they should be specifically addressed in the Act (e.g. lien bonds, holdback release bonds).

### Enforcement and penalties

The current Act does not impose any penalties for non-compliance, with the exception of section 57 (costs consequences for failing to take the least expensive course) and subsection 3(2) (which makes unauthorized use of trust funds a category F offence). Given that general non-compliance appears to be a widespread problem, one of the questions we are considering is whether adding further penalties or some other sort of enforcement mechanism would be useful. (For example, some jurisdictions have implemented licensing schemes as a means of allowing for more direct regulation of contractor behavior.) We are also considering whether to retain the offence provision.

So far, we suspect that the best way to increase compliance in a general sense is to make the Act easier to understand and more reflective of the realities of the modern construction industry. If, however, our readers think otherwise, we would be happy to hear their comments on this point.

### **Prompt payment**

One of the key concerns raised by stakeholders across Canada and around the world is the persistent and worsening problem of delinquent payment. This issue is not addressed by existing lien legislation, which deals only with payment default.

The prompt payment issue involves two distinct sub-issues, each of which requires a distinct remedy:

- delays in “ordinary course payments”;
- delays arising out of payment disputes and the lack of an effective, timely mechanism of dispute resolution, which can quickly lead to project “gridlock”.

A number of jurisdictions (e.g. United States, Ireland, Australia, New Zealand, Singapore, Hong Kong and Malaysia) have adopted, or are considering, legislation designed to encourage promptness of payment. Prompt payment has been in place in the United Kingdom for over 20 years and has apparently been very successful. (We note that the UK does not use a lien and holdback system.)

The common objective of all the international schemes is to maintain the flow of cash down the construction pyramid. Common features include:

- the right of a contractor or subcontractor to make claims for progress payments;
- an obligation on the owner or general contractor to evaluate a claim for payment within a reasonable period of time (generally 30 days);
- the right to give written notice of a disputed claim for payment, and the obligation to give reasons for the dispute;
- penalties, such as interest, on late payments;
- the right of a contractor or subcontractor to suspend performance for non-payment;
- the prohibition of conditional payment provisions;
- a right to refer disputes arising under the contract to adjudication.

In May 2017, Canada made some progress toward prompt payment at the federal level with the passing of Senate [Bill S-224](#), *An Act respecting payments made under construction contracts*. It is currently awaiting first reading in the House of Commons. On the provincial front, Alberta Infrastructure began implementing prompt payment in its contracts in April 2016. In April 2017, the Ontario Expert Review recommended (and the government later accepted) that prompt payment be adopted in Ontario. That scheme, modeled on the one in place in the UK, will operate alongside Ontario’s existing lien and trust schemes, will apply to both the public and private sectors, and will be implied into all construction contracts that do not contain equivalent terms.

Another important element of the proposed Ontario scheme is the introduction of a system of mandatory adjudication for certain payment-related disputes. This is also modeled on the UK scheme, which is described as “pay now, argue later”. When originally implemented in the UK, adjudication was an unprecedented step, but 20 years later it is reported to be well established, well understood, and very

successful. Adjudication has substantially reduced the workload of the court and decreased the overall volume of construction litigation.

The UK scheme has also served as a model internationally. The only international jurisdiction to *not* include mandatory adjudication as part of its prompt payment scheme is the United States. There, the parties are left to resolve their disputes through ordinary litigation, which has led to questions about the efficacy of the entire prompt payment scheme. Without a mechanism of rapid payment dispute resolution, the purpose of prompt payment legislation is essentially defeated, as projects can quickly become mired in payment-related disputes.

As noted above, we intend consider this issue in greater detail in the next issue of the *Law Reform Notes*. Between now and then, we hope that readers will have the opportunity to familiarize themselves with key background resources, most importantly the report of the Ontario Expert Review (Chapters 8 and 9). It explains the proposed Ontario scheme and offers a thorough analysis of the key issues, including stakeholder views and a jurisdictional analysis.

## **Conclusion**

As is clear from the above, this is a comprehensive review of the Act, which we hope will ultimately result in legislation that is more effective, efficient and accessible. To that end, we reiterate our interest in feedback on any of the issues and potential solutions raised above. We also acknowledge that, despite the length of this note, there are likely issues that are important to readers but that were not raised here (e.g. limitation periods, forms, procedural refinements generally, “housekeeping” issues (e.g. repealing section 11, relating to dower)). We invite comment on those as well.

Finally, given the especially practical nature of the *Mechanic’s Lien Act*, we encourage readers to share not only their comments and concerns, but also how these might be addressed in a way that makes sense “on the ground”.

## **Resources**

For more information and discussion on many of the issues described above, we refer readers to the following resources:

### Ontario Construction Lien Act Review

- [Striking the Balance: Expert Review of Ontario’s Construction Lien Act \(Final Report, April 2016\)](#)
- [Background documentation and stakeholder submissions](#)

### New Brunswick

- [The Mechanics’ Lien Act: Time for Repeal? \(Law Reform Branch – Discussion Paper, July 1992\)](#)

### Nova Scotia

- [Builders’ Liens in Nova Scotia: Reform of the Mechanics’ Lien Act \(Final Report, June 2003\)](#)
- [Builders’ Lien Act \(Final Report, March 2013\)](#)

### British Columbia

- [Builders Lien Act Reform Project Backgrounder](#) (project is ongoing)
- [Mechanics’ Lien Act: Improvements on Land \(1972\)](#)

- [Report on Builders Liens and Arbitration \(2002\)](#)

Ontario Bar Association, Construction and Infrastructure Law Section

- [An Insider's Look into the Construction Lien Act Review Process and Recommendations](#) (login required)

*Responses to any of the above should be sent to the address at the head of these Notes or by e-mail to [lawreform-reformedudroit@gnb.ca](mailto:lawreform-reformedudroit@gnb.ca). We would like to receive replies no later than February 15, 2018, if possible.*

*We welcome suggestions for additional items which should be studied with a view to legislative reform.*