

January 2010

OWNER

The Construction Lien Act allows a person to lien an owner's interest in an improvement. Is an "owner" just the registered owner of land or is "owner" defined more broadly? Can a mortgagee be an owner? If so, what affect does that have on the priority sections of the Act? Parkland Plumbing v. Minaki Lodge Resort 2002 Inc., a 2009 decision of the Ontario Court of Appeal, answers these questions.

History

Minaki Lodge, a resort north of Thunder Bay, has had a troubled history. CN developed it, but it ultimately became a money pit and CN jumped ship. Ultimately, the Ontario government became involved (Northern tourism and all that) and sunk millions into it. Then, in early 2002, after subsequent owners suffered similar fates, Mr. Archer purchased the lodge for \$1.95 million through Minaki Lodge Resort 2002 Inc. and financed it, in part, through Celestine Mortgage Corp. Archer was the sole shareholder, director, and officer of Minaki and the sole officer and a director of Celestine. His wife was Celestine's other director and its sole shareholder.

Archer, through Minaki, arranged for extensive work to be done on the lodge. The first work commenced in April 2002; the first lien was registered in May 2003 and many liens followed. Celestine ultimately advanced approximately \$5 million.

A fire destroyed the lodge in October 2003. What happened to the insurance proceeds, you ask? There were none. Minaki did not bother to place insurance and Celestine did not force Minaki to do so.

Celestine commenced power of sale proceedings in November 2003 and the matter went to trial based on the issues of ownership and priorities. The trial judge held in favour of the lien claimants and a trustee ultimately sold the land and what remained of the lodge for \$1.9 million. The Divisional Court reversed the trial judge's decision and the lien claimants appealed to the Court of Appeal.

Issue

The case revolved around the issue of whether Celestine was an owner under the Act. If it was, then, under section 78(1) of the Act, the lien claimants had priority over all other interests, subject to other provisions of section 78 that we will discuss.

The Court noted that there were three prerequisites for a person to fall within the definition of "owner" under s. 1(1) of the Act: *"(i) the person said to be an owner must have an "interest in a premises"; (ii) that person must have "requested" an improvement to the premises; and (iii) the improvement to the premises must have been made on the credit, on behalf of, with the privity or consent of, or for the direct benefit of the person said to be an owner."*

In order to determine whether Celestine satisfied the requirements, the Court dealt with the concept of "lifting the corporate veil."

Peek

As a rule, every corporation has a separate legal existence and is distinct from its shareholders and other corporations. Like every general rule, it has exceptions. A court

can ignore the corporate framework and regard a corporation as the agent or vehicle of its controlling shareholder if enforcing the separate entity principle would yield a result that was flagrantly opposed to justice. However, the courts cannot exercise a general discretion simply to do what they feel is right. The facts must meet two criteria. First, the entity to be fixed with liability must completely dominate the corporation such that the corporation does not function independently. Second, the conduct of the dominating entity must be akin to fraud that would unjustly deprive claimants of their rights.

The trial judge made critical findings of facts that the Court had to accept, given that there was some evidence to back up those findings.

1. Archer signed the mortgage on behalf of Minaki. Archer controlled all corporations. Only Archer acted for Celestine regarding the development.
2. Celestine and Archer made payments directly to Minaki's creditors and treated these payments as advances under the Celestine mortgage.
3. Neither Archer nor Celestine took any steps to enforce Celestine's payment rights under its mortgage until after the commencement of the lien actions.
4. None of Archer's dealings with the various corporations was at arm's length.
5. Archer failed to act in a commercially reasonable fashion regarding the insurance and willingly compromised the interests of the lien claimants. Archer was content to do so because he assumed that the Celestine mortgage had priority to the extent of the cost of the land.
6. Contrary to ordinary commercial practice, when Ce-

lestine advanced funds it did not subsearch title to ensure that there were no liens. Further, Celestine continued to advance funds even after the fire and even though Minaki had never made any payments on the mortgage.

7. Minaki and Celestine were indistinguishable.

The Court decided that these findings demonstrated that Archer completely dominated Celestine. However, instead of dealing with the second criteria (i.e. an act akin to fraud), the Court moved on to the statutory definition of owner.

Criteria

The Court first held that Celestine had an interest in the lodge. The Act defines "interest in premises" as an estate or interest of any nature. The Court felt that this was wide enough to encompass a mortgage.

Did Celestine "request" that work be done on the improvement? Although Celestine never had any direct dealings with the lien claimants, this did not determine the issue. If it did, then any developer could insulate itself from liability by incorporating a straw corporation to contract with the contractors. Accordingly, a request for work could be inferred from all the circumstances. The Court referenced the trial judge's findings of fact to note that Archer and Celestine did not operate independently and were indistinguishable. Further, Celestine had the right to approve plans and designs for the lodge and could have been involved directly with the improvements. All of this was sufficient for the Court to find that Celestine requested the lien claimants to provide the work.

Finally, the Court latched onto one criterion in the third requirement for ownership. Was the improvement made for the direct benefit of Celestine? The Court again referred to the findings of fact and the lifting of the corporate veil analysis to conclude that Minaki and Celestine constituted a joint enterprise

with Archer to redevelop the lodge. Accordingly, the redevelopment was carried out for Celestine's direct benefit.

Priority

Section 78(3) provides an exception to the general priority for liens given in section 78(1). It gives priority to "mortgages or other agreements affecting the owner's interest in the premises" registered before the time the first work was done on the improvement. The priority is for the actual value of the land when the first work begins.

Giving a mortgagee priority for the value of the land makes sense when a mortgagee is separate from the owner. However, once the mortgagee is also one of the owners, by simply substituting mortgagee for owner in the definition, the section would read that a mortgage would have priority if it affected the owner's (i.e. mortgagee's) interest. This interpretation

would be silly. Accordingly, the Court held that this section relates only to a derivative interest (i.e. when a mortgagee takes its interest from the interest of an owner, not when the mortgagee is an owner).

Result

Since Celestine was an owner, section 78(1) of the Act gave the lien claimants priority over the monies from the sale of the lodge and section 78(3) did not apply to give any priority to Celestine's mortgage.

Smell

The Court went to great lengths to state that Archer's failure to place appropriate insurance on the lodge was not the sole reason for its decision to hold Celestine to be an owner. However, that was the one fact of the case that cried out for justice. Archer decided to risk a fire and the lien claimants be damned. No court would willingly reward Archer's unreasonable behaviour.

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