

BUILDERS' LIENS AND STAYS OF PROCEEDINGS IN RECEIVERSHIPS

Pandemic-related debt, high interest rates, high energy costs, shortages of labour and rising costs of equipment and materials could all contribute to a rise in the number of insolvencies in the construction industry. A contractor becoming insolvent can have a number of impacts on both the project owner, the subcontractors and suppliers. This article discusses a particular issue related to a contractor becoming insolvent after subcontractors have filed builders liens against the project property.

The principal statute governing insolvency proceedings in Canada is the *Bankruptcy and Insolvency Act*¹ (the "**BIA**"). The BIA is federal legislation that sets out three types of insolvency processes, including a receivership process. While typically initiated by a secured creditor holding security over all or some of the debtor's property, a receiver appointed by the court under the BIA must administer the receivership for the benefit of all the creditors. The receiver exercises powers granted to it by court order, which often include the power to take control of the debtor's property, to operate and manage it or to dispose of it. These powers are intended to assist creditors with enforcing their debt

claims by maximizing the amount that can be recovered from the insolvent party's assets. To help the receiver maintain control over the insolvent party's assets, a court order appointing a receiver will usually include a stay (a pause) of proceedings preventing actions against the debtor or its property starting or continuing without leave of the court.

Once a contractor becomes insolvent, it is very likely that the contractor has left subcontractors and materials suppliers unpaid. These unpaid subcontractors and suppliers may consequently register builders liens against the land on which the project is being carried out pursuant to the British Columbia's *Builders Lien Act*² (the "**BLA**").

Subcontractor builders liens are usually the general contractor's responsibility. The head contract between the owner and the general contractor for a project will typically include the obligation of the general contractor to discharge any liens registered by subcontractors or suppliers claiming under the general contractor. To fulfill this obligation, a general contractor will often choose to either pay the lien claimants or apply to court to have the claims of liens cancelled upon giving security for the payment of the

claims under section 24 of the BLA³. An insolvent contractor whose property is administered by a receiver is unlikely to do this. In such circumstances, the owner may seek to rely on its rights to seek a removal of the claims of liens against its interests in the lands of the project under the BLA. One rather straightforward remedy available to project owners under the BLA is the remedy provided under section 23 of the BLA. Generally, under section 23 of the BLA, an owner may, on application to the court, pay into court the lesser of:

- a) the total amount of the claim or claims of liens filed, and
- b) the amount owing by the owner to the contractor through whom the liens are claimed provided the amount is at least equal to the required holdback in relation to the contract⁴.

Payment into court pursuant to a court order under section 23 of the BLA discharges the owner from liability in respect of the claims of liens filed. The court order will provide for the removal of the claims of liens, and the money paid into court will stand in place of the land. The lien claimants, seeking satisfaction of their claims, will be entitled to claim against the funds paid into court. If the lien claimants are not entitled to all the funds, then the remainder may be claimed by the general contractor.

Where there is a receivership, a question is raised as to whether the owner's right to seek the remedy under section 23 is impacted by the stay of proceedings provided in a receivership order made in respect of owner's general contractor. It may appear the court proceeding intended to be commenced by the owner to remove the claims of liens is a proceeding commenced in respect of property of the insolvent contractor or against the contractor, and thus, caught by the stay of proceedings order. If this were the case, the owner

would need to take the additional step of obtaining the receiver's consent or leave from the court.

There is, however, legal authority supporting the position that the stay of proceedings provided in a receivership order will not prevent an owner from applying to the court to remove claims of liens in exchange for payment into court of the holdback and any extra amount owing to the contractor under the contract. This position relies on the money being paid into court being distinguished from the insolvent party's property and the payment into court not otherwise prejudicing the insolvent contractor's rights.

In the case of *D&K Horizontal Drilling (1998) Ltd. (Trustee of) v Alliance Pipeline Ltd.*⁵, the owner was ordered to pay into court, pursuant to the applicable builders lien legislation, the amount of the statutory holdback in respect of the contract between the owner and the bankrupt contractor, and the balance of the monies payable to the bankrupt contractor over the statutory holdback. Upon payment into court of the funds, the claims of liens were to be discharged from title to the lands. The owner paid the required monies into court, and the registered liens were removed from title. The trustee in bankruptcy appointed to administer the bankrupt contractor's property challenged the lien claimants' entitlement to payment of their liens out of the funds paid into court. The trustee in bankruptcy contended that it had a prior claim to those funds, arguing that the balance of the contract price was an account receivable of the contractor, and as such, was payable to the trustee for distribution to the contractor's creditors. The Court of Appeal disagreed with the trustee, holding that the money paid into court, to the extent of the lien claims, was not the property of the bankrupt contractor. The Court of Appeal reasoned that the monies paid into court by the owner stood in place of the land and for the subcontractors' rights to

sue the owner personally for the satisfaction of their claims of liens. This was so because the owner had under the provincial builders lien legislation an obligation to subcontractors to maintain a holdback of 10% of the value of the contract. If the owner did not discharge its obligation, it could render it liable to the subcontractors.

In the case, the proceeding commenced against the contractor was a bankruptcy proceeding, another type of proceeding under the BIA, which entailed the appointment of a trustee in bankruptcy as opposed to a receiver. However, the principle stated by the Court of Appeal in the case holds true in a receivership proceeding commenced against an insolvent contractor despite differences between bankruptcy proceedings and powers of trustees in bankruptcy and receivership proceedings and powers of court appointed receivers.

The court distinguishing between money to be paid into court as security for unproven claims by subcontractors from money that is unquestionably owed to the insolvent general contractor is significant to an owner seeking to discharge liens and to subcontractor lien claimants who want to preserve their secured claims in relation to a particular project despite many other creditors seeking to recover monies from the general contractors. Owners should nevertheless seek legal advice regarding their remedies if a contractor's insolvency has caused builders liens to linger on title.

February, 2024

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Footnotes:

1. *Bankruptcy and Insolvency Act*, RSC, 1985, c B-3
2. *Builders Lien Act*, SBC 1997, c 45
3. *Ibid* at s. 24
4. *Ibid* at s. 23
5. *D&K Horizontal Drilling (1998) Ltd. (Trustee of) v Alliance Pipeline Ltd*, 2002 SKCA 145



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