

'Breach of Trust' could make you liable

In the construction industry, using a corporation to conduct business is not a foolproof way to avoid personal liability. While liens under the Construction Lien Act are relatively well known, the 'trust remedy' is sometimes overlooked, with serious consequences.

If a company runs afoul of the trust provisions of the Construction Lien Act, directors, officers and other persons who have effective control of the corporation, or its relevant activities, may find themselves personally liable.

All amounts received by an owner, contractor or subcontractor in connection with a construction project are impressed with special qualities. Everyone in the construction pyramid who comes in contact with the project trust funds has certain obligations to the beneficiaries of the trust fund. Failure to meet those obligations constitutes a 'breach of trust.' In the case of a corporation, the officers, directors, agents and key employees of the company may be personally liable for the breach of trust.

Obligations of an owner's trusts

A number of different trust funds will exist during the life of a typical construction project, each of which may become a trap for the unwary.

All amounts received by an owner that are to be used to finance the construction is a trust fund which the owner cannot use for

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any purpose until the contractor hired to make the improvement has been paid in full by the owner. Where the contractor is to be paid upon the issuance of a certificate by a payment certifier, or where a certificate of substantial performance has been issued, then any amount received by the owner thereafter is a trust fund which cannot be used for any other purpose until the contractor is paid in full.

If an owner sells the improved property, the net proceeds of sale also constitute a trust

fund and the owner cannot use those proceeds for any purpose until the contractor has been paid in full.

More than 10 years ago, a commercial landlord and its principal experienced firsthand the onerousness of the owner's trust obligations. Here are the short strokes of that case.

Westcola hired a contractor to rehabilitate its underground parking garage. A certificate of substantial performance of the work was issued. Westcola received rents, paid utility bills, maintenance costs, insurance, property taxes, and other overhead expenses in the normal course, just like any landlord would.

The unpaid contractor successfully sued Westcola and its principal for breach of trust, since the monies in the owner's hands when a contract has been certified to be substantially performed, or received by the owner thereafter, is a trust fund in an amount equal to the unpaid price of the substantially performed contract for the benefit of the contractor.

Westcola was surprised to learn that, in this case, the rents collected were trust funds and, in the absence of payment, the landlord was liable for breach of trust. The principal of Westcola was surprised to learn that he was personally liable for the unpaid contract price.

Contractor's and sub-contractor's trusts

A contractor hired by an owner also has

trust obligations. All amounts received by the contractor on account of the work constitute trust funds for the benefit of the trades and suppliers who worked on the project and who are owed amounts by the contractor. The contractor is prohibited from using any of the money received from the owner until all of its subcontractors and suppliers have been paid in full for what they supplied to the project.

A breach of trust is committed where project funds are used to pay any kind of overhead expense (rent, insurance, lease payments, legal and accounting expenses, general wages etc.) before the labour and materials in connection with the specific project are paid in full.

Similarly, sub-contractors and suppliers, at all rungs of the construction ladder, must hold the amounts they receive, and not use the funds for any purpose, until their trades and suppliers have been paid in full for the project.

Each project must be looked at separately and 'robbing Peter to pay Paul' is definitely a breach of trust if the 'borrowed' monies are not replaced and suppliers of services and materials remain unpaid.

Personal liability

Every director or officer, and any person who has effective control of a corporation or its relevant activities, who acquiesces in conduct that he or she knows or reasonably ought to know, amounts to a breach of trust by the corporation, is personally liable for the breach of trust.

When determining who has control of a corporation, the courts may disregard the form of any transaction and the separate corporate existence of any of the entities involved. With the help of the trust provisions of the Construction Lien Act the corporate veil, which normally affords good protection against personal liability, can successfully be lifted in the construction industry.

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Baxter awarded for excellence

Mississauga's Baxter Corporation has been named among the 2011 recipients of the prestigious Canada Awards for Excellence, with a Silver Award for outstanding achievement in Excellence, Innovation and Wellness.

Presented annually by Excellence Canada (formerly National Quality Institute), the Canada Awards for Excellence is an annual awards program to recognize business excellence in quality, customer service, and a healthy workplace.

This award is based on Excellence Canada's Progressive Excellence Program (PEP) for Quality and Healthy Workplace, which is a target-driven, incremental approach to applying excellence criteria.

To receive the Silver recognition, organizations must be at the equivalent of PEP Level 3.

"Each day at Baxter we strive to help advance the best in healthcare for Canadian patients and professionals and are honoured to have earned this recognition of Baxter's continuing excellence journey," says Barbara M. Leavitt, president, Baxter Corporation.

"As we continue on this path to business excellence, we remain committed to a healthy workplace that fosters integrity and innovation, and helps us consider what truly adds value and contributes to our vision of saving and sustaining lives."

Excellence Canada will present the Silver Award for Excellence, Innovation and Wellness to Baxter at the 2011 Canada Awards for Excellence ceremony on November 1, in Toronto.