

Landlord's and Tenant's Liability for Improvements under the *Construction Lien Act*

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Many contractors assume that their work on leasehold improvements automatically gives them a right to lien the landlord's interest as well as the tenant's interest in the improved property. In many cases, however, the landlord's interest cannot properly be the subject of a construction lien, even where the landlord has provided a "leasehold improvement allowance", absent facts that support a finding that the landlord is the statutory owner as defined under the Ontario *Construction Lien Act*, R.S.O. 1990 c. C.30 (the "Act").

There are only two ways for a contractor who has done work on leasehold improvements to lien the landlord's interest. One way is to provide the landlord with notice up front before the work is done, pursuant to section 19(1) of the Act. The other is to argue that the landlord is an owner under the Act. Under section 19(1) of the Act, where the owner is a tenant, the interest of the landlord will also be subject to the lien if (a) the contractor gives the landlord written notice of the improvement before it is made, and (b) the landlord fails within 15 days of receipt of that notice to provide notice to the contractor that it assumes no responsibility for the improvement. The notice to be given pursuant to this provision has to be "sufficiently distinct and memorable"¹ to allow a landlord to know when the 15-day period to disclaim responsibility has begun. The courts have held that such matters as the landlord's attendance at meetings, review of plans, or simple awareness of the work being done are not enough to constitute notice under this provision of the Act. In this regard, any notice must clearly signify the potential liability to the landlord.²

In *Lincoln Mechanical Contractors. v. Cardillo*,³ the defendant RioCan Holdings Inc. ("RioCan") was the owner of a commercial plaza whose tenant was a numbered company operating as Premier Fitness ("Premier"). There were provisions in the lease agreement with respect to improvements that were to be made to the leased premises by each of RioCan, the landlord, and Premier. RioCan agreed to pay Premier a leasehold improvement allowance of approximately \$2.2 million to subsidize the cost of renovations, which represented approximately one-half of the cost of the improvements to be made by Premier. Premier hired the plaintiff mechanical contractor, Lincoln, to do HVAC work but did not pay it in full and Lincoln filed a claim for lien against both the landlord and the tenant, claiming that RioCan was an owner as defined in the Act. Lincoln further alleged that the landlord had held back approximately \$234,000 of the leasehold improvement allowance funds and claimed that, because RioCan was an owner, pursuant to section 7 of the Act these funds were impressed with a trust and should have been applied to its outstanding account. Instead, the balance of the leasehold improvement allowance was paid by RioCan to Premier or set off against monies owed by Premier to RioCan.

The question before the Court was whether the totality of the circumstances permitted an inference that the landlord had requested that the work be done. Premier argued that the lease provided that it would deliver a contractor's quote outlining the scope and cost of the work, as well as a complete set of drawings and specifications, to RioCan. The work, drawings, and specifications would then be subject to RioCan's approval. The lease also set out conditions regarding the payment of the leasehold improvement allowance, including a provision that the work would be completed to RioCan's satisfaction. The landlord argued that there was no privity of contract or direct dealings

¹ See *Pinehurst Woodworking Co. v. Rocco*, [1986] O.J. No. 41 (Ont. Div. Ct.) as cited in *1276761 Ontario Ltd. v. 2748355 Canada Inc.* 2006 CarswellOnt 5392, 55 C.L.R.T. (3d) 54, at para. 11

² *1276761 Ontario Ltd. v. 2748355 Canada Inc.* (2005) 44 C.L.R.(3rd) 284 (Ont. S.C.) aff. 2006, 55 C.L.R. (3rd) 54 (Ont. Div. Ct.).

³ 2011 ONSC 664.

between the lien claimant and the landlord. There was also no evidence that RioCan had ever received a quotation, drawing, or specification in respect of the HVAC contractor's work. The court ruled that even though the landlord had certain rights under its contract with the tenant, without evidence that the rights were exercised this fact did not support an inference that the landlord requested that the work be done. The court determined that for the work to be done for RioCan's benefit, there must be more than "the benefit to landlord as a reversioner, and in the present case any benefit to RioCan would be the benefit as a reversioner".

In *Haas Homes Ltd. v. March Road Gym and Health Club Inc.*,⁴ the court held that the landlord's agreement to contribute to the cost of the tenant's fit-up was an insufficient ground for a finding that the landlord was the statutory owner. The lien claimant delivered a quotation to the tenant, and dealt with the tenant only for payment and claims for extras. Representatives of the landlord were on the scene during the course of the lien claimants work who exercised a general supervisory function over all contractors engaged in the work, including the landlord's own general contractor and subtrades, as well as contractors for new tenants who were fitting up their own premises. The court determined that there was not sufficient proof of significant direct dealing between the landlord and the lien claimant to establish that improvements were made to the property with the landlord's "privity and consent".

What can an unpaid contractor do when the tenant in a commercial lease abandons the leased premises? The ultimate remedy of a lien claimant against a leasehold interest is to sell the remaining term for which the tenant holds the land and its interest in the building, if any. Such remedy is of little appeal to the unpaid contractor. Another option might be to argue that the financing of tenant improvements constitutes trust funds under section 7 of the Act and use section 13 to hold anyone liable who might have diverted such funds to other start-up costs of the commercial tenant at that location.⁵ The easiest way for a contractor to ensure that the landlord is subject to the obligations imposed upon owners under the Act is to provide notice to the landlord in accordance with section 19(1) before the work starts. In the event that the landlord gives the contractor timely written notice that it assumes no responsibility for the improvement to be made, the contractor can then decide whether or not it wants to proceed with the work for the tenant without some additional form of security.

⁴ (2003), 29 C.L.R. (3rd) 243 (Ont. S.C.)

⁵ CCF Structural Contracting Ltd. v. Westcola Holdings Inc., [2000] 48 O.R. (3d) 417 (C.A.) as reported by David Debenham in his paper entitled "Using the Construction Lien Act to Your Client's Advantage: Do you Need a Magic Bullet? Seven Simple Solutions to Persistent Pernicious Problems in your Practice".

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