SUPREME COURT OF NOVA SCOTIA IN BANKRUPTCY & INSOLVENCY

Citation: *Royal Bank of Canada v. 2M Farms Ltd.*, 2017 NSSC 235

Date: 20170906
Docket: Hfx No. 425907
Registry: Halifax

Between:

Royal Bank of Canada

Applicant

v.

2M Farms Ltd.

Respondent

Decision

Judge: The Honourable Justice Gerald R.P. Moir

Heard: May 25, 2013, in Halifax, Nova Scotia

Counsel: Gavin D.F. MacDonald and Meryn Steves, for the Applicant
Tim A.M. Peacock, for the Intervenor, National Building Group Inc.

Moir, J. :

[1] The Royal Bank and the receiver of 2M Farms Ltd. move for a determination of the priority of charges against 2M Farms' commercial property in Berwick. The bank claims that its personal property security and its land mortgage are both first in time and first in priority. National Building Group Inc. claims that its builders' lien has priority over the mortgage by virtue of the bank's consent.

[2] The mortgage was executed late in August 2012. It and the personal property security instrument were registered under the *Land Registration Act* and the *Personal Property Security Act* in early October 2012. The claim for lien was registered at the end of November 2013. The bank is owed about one million dollars, National Building about $130,000. The receiver realized $210,000 for land at 94 Parker Condon Road in Berwick and $159,750 for equipment. The $210,000 is in trust.

[3] The only issue turns entirely upon the application of s. 8(3) of the *Builders' Lien Act*:

> (3) Where the land upon or in respect of which any work or service is performed, or materials are placed or furnished to be used, is encumbered by a prior mortgage or other charge and
>
> (a) the selling value of the land is increased by the work or service, or by the furnishing or placing of the materials; and

> (b) the mortgagee consents to the performance of such work or service or the furnishing, or placing of such materials,
>
> the lien shall attach upon such increased value in priority to the mortgage or other charge.

[4] The evidence on consent comes from Ms. Angela Franey of Berwick, a sales representative and project manager with National Building Group. Her evidence is uncontested.

[5] She wrote to Mr. J.T. (Joe) McGrath at the Berwick branch of the Royal Bank on June 27, 2012. Mr. McGrath is an account manager for "Royal Bank of Canada Southwest Nova Scotia Agriculture/Business Markets". He has an office in the Berwick branch.

[6] The email advised Mr. McGrath that "the building" had been ordered on a $30,000 deposit. She asked "When would be the earliest to receive our next draw?" The price was to be $645,025 payable at $175,000 initially, $350,000 on July 26, 2012, $120,000 when foundation and frames were complete, with the balance on completion.

[7] Mr. McGrath responded by email the same day writing, "between RBC and ACOA sufficient funds have been approved to cover the cost of the project…". He referred to the project as "Peter Heeres – 2M Farms", which signifies the

construction now mortgaged and liened. The payment schedule was to be between the builder and the owner.

[8] Ms. Franey requested, and received, a letter confirming financing. The letter is signed by Mr. McGrath, captioned 2M Farms Ltd. and dated September 6, 2012. It reads:

> This letter is to confirm that RBC has financing approved and in place, in the amount of $650,000.00, related to the construction of a potato storage building located in Somerset Nova Scotia for the above company.
>
> The exact date when funds will be released is not known but should be shortly.
>
> If you require additional information, please contact the undersigned.

The reference to Somerset is an error. Mr. McGrath meant Berwick.

[9] The evidence on performance of work, supply of materials, and advances comes primarily from an affidavit of James DeVries, president of National Building Group. Mr. DeVries' affidavit was filed for another motion, but counsel for National Building Group gave notice in his brief that his client wished to refer to the affidavit. Therefore, Rule 39.06 applied.

[10] The building contract is dated July 7, 2012 and it was amended on August 12, 2013. Work was completed a year later, on September 30, 2013. Payments to

the builder came from advances by the bank, but there was an outstanding balance of $131,597.

[11] The question is whether the communications from Mr. McGrath are within s. 8(3)(b). The facts are simple enough. The difficultly is to correctly interpret the phrase "the mortgagee consents".

[12] The *Mechanic's Lien Act* was overhauled and renamed *Builders' Lien Act* by S.N.S. 2004, c. 14. Section 8 and its significant textual context remained the same.

[13] The first *Mechanics' Lien Act* included a similar provision to the present section 8. It applied to "a mortgage or other charge, existing or created before the commencement of the work or of the placing of the materials". It gave the lien priority to the extent of a sum by which the "selling value thereof has been actually increased by the improvement". However, the consent had to be to the lien rather than the performance, "…provided that the mortgagee or holder of such charge consent to such lien charging the land…": *Liens in Favour of Mechanics*, R.S.N.S. 1884, c. 85, s. 4.

[14] The provision was dropped altogether by the next iteration of the statute, S.N.S. 1899, c. 29. The legislative intent was to leave priorities to the *Registry Act*:

Silver v. R.R. Seeton Construction Ltd., [1977] N.S.J. 734 (O'Hearn, Co. Ct. J.) para. 32.

[15] The provision was restored, in exactly its present wording, by *The Mechanics' Lien Act*, S.N.S. 1915, c. 2, s. 8.

[16] As will be seen, the courts determined that what is now s. 8(3) is in conflict with s. 15(1):

> The lien shall have priority over all judgments, executions, assignments, attachments, garnishments and receiving orders recovered, issued or made after the lien arises, and over all payments or advances made on account of any conveyance or mortgage after notice in writing of the lien to the person making such payments or after registration of a claim for such lien as hereinafter provided.

[17] Other Canadian jurisdictions have had provisions for priority over a "prior mortgage" to the extent the builder improves the value, but without our requirement for consent. This was the situation in Ontario before 1922 and in Manitoba in 1972. Some early decisions in Ontario and a decision of the Manitoba Court of Appeal in 1972 influenced Nova Scotia courts. Let us start with the Manitoba decision.

[18] *Northern Electric Co. v. Frank Warkentin Electric Ltd.*, [1972] M.J. 21 (C.A.) was written by Dickson, J.A. later C.J.C., except for a dissent on a minor point by one judge on a five member panel.

[19] An apartment block was being constructed under a ground lease and a leasehold mortgage. The mortgage was recorded before work began. The mortgagee advanced funds until it got notice of mechanics' liens.

[20] Subsection 5(3) of the Manitoba *Mechanics' Liens Act* provided for a builder to rank ahead of a prior mortgagee to the extent the work or materials improved the value of the land. And, s. 11(1) provided priority over advances made after the mortgagee got notice of a lien, or the lien was registered. Similar to our s. 8(3), but without the requirement for consent, and our s. 15(1).

[21] The mortgage was executed and registered in August 1968, and the work began in September 1968. It was argued "if the land upon which the work is done is encumbered by a mortgage created before the commencement of the work… that mortgage has priority over a lien… to the extent of the actual value of the land at the time the improvements were commenced" (para. 9). In the circumstances of the ground lease, there would be no value before construction.

[22] Justice Dickson wrote, "I do not agree." (also, para. 9) He explained at para. 10:

> Let us accept, arguendo, that "land" and "leasehold" are synonymous for present purposes, that the leasehold interest of Victoria Arms was of no value at the time it was mortgaged to Canada Life, and that the Canada Life mortgage was a "prior" mortgage. None of these circumstances serves to negate section 11(1) of the Act,

> the effect of which is to permit a mortgage, whether "prior" (one which exists in fact before the first lien arises) or "subsequent" (all mortgages which are not prior mortgages) securing future advances to gain priority over mechanics' liens prior to notice, or registration, of lien… [authorities omitted]

[23] *Northern Electric Co. Ltd. v. Manufacturers Life Insurance Co. and Metropolitan Projects Ltd.*, [1974] N.S.J. 255 (S.C., A.D.) reversed on other grounds [1977] 2 S.C.R. 762 also involved the construction of an apartment building on ground lease and leasehold mortgage financing. Advances were made until the mortgagee got notice of liens or they were registered. Among other things, the trial judge held "…by virtue of s. 7(3) the lienholders had priority over the first mortgage to the extent of an increased selling value…" (para. 6).

[24] Justice Coffin wrote for the Appeal Division. He followed the Manitoba Court of Appeal, saying at para. 39:

> Mr. Justice Dickson then dealt with the apparently inconsistent application of what is our s. 7(3) and rightly, in my respectful opinion, held that the equivalent Manitoba section did not apply to a mortgage where the advances were made after work began, as in our case. Any other interpretation would render meaningless what is our s. 14(3).

This encapsulates, and adopts, the interpretation of the equivalent in Manitoba of our present s. 8(3) and s. 15(1). Subsection 8(3) does not apply to a mortgage under which advances are made after work begins, typical construction financing.

[25] As I said, some decisions in Ontario before it changed its statute in 1922 influenced the interpretation of s. 8(3) here. The builders' lien jurisprudence in Nova Scotia owes a great deal to the scholarship of Judge Peter O'Hearn. He referred to the early Ontario decisions in *Riviera, The Home of Siding, a division of Riviera Home Improvements v. Chalker Properties Ltd.*, [1982] N.S.J. 65 (Co. Ct.).

[26] Judge O'Hearn described s. 8(3) this way at para. 4:

> Again, s. 7(3) provides that where the land is incumbered by a prior mortgage or other charge and the selling value of the land is increased by the provision of services or materials, the lien attaches to the increased value in priority to the mortgage or other charge if the mortgagee has consented to the provision of the services or materials.

[27] Judge O'Hearn noted that the Ontario provision did not require consent of the mortgagee. He referred to two decisions of the Ontario Chancery Division and two of the Ontario Court of Appeal, and he endorsed this summary: "a 'prior mortgage' is ordinarily 'a lump sum mortgage fully advanced before commencement of work on the land' " (also, para. 4).

[28] I am bound by *Northern Electric Co. Ltd. v. Manufacturers Life Insurance* and its holding that s. 8(3) does not apply to a mortgage where the advances were made after work began. Judge O'Hearn's opinion, that the subsection ordinarily applies to a lump sum mortgage fully advanced before commencement of work, has

much weight. However, the present motion was argued primarily on the meaning of "the mortgagee consents" and, at that, with emphasis on "consents". Let us look at some authorities on that narrow point.

[29] Judge McLellan wrote about the meaning of consent in s. 8(3) in *Burns (c.o.b. Burns' Handymen) v. Zelco Enterprises Ltd.*, [1982] N.S.J. 156 (Co. Ct.) affirmed [1983] N.S.J. 447 (S.C., A.D.). That was a case in which a vendor was deemed to be a mortgagee. It did not involve a construction mortgage.

[30] The judge said at para. 13 that the "issue of consent" is "for decision for the first time in Nova Scotia". He provided a rendition of relevant facts and his conclusion that they establish consent. Justice Grant referred to this decision, saying "a broad interpretation was given to the term 'consent' " *Atlantic Trust Co. of Canada v. Warm and Cosy Renovations and Development Ltd.*, [1988] N.S.J. 485 at para. 12. He found consent by a person who held a vendor's lien. Again, the case did not involve construction financing.

[31] *Glasswall Ltd. v. 2009861 Nova Scotia Ltd.*, [1994] N.S.J. 133 (S.C.) affirmed [1994] N.S.J. (C.A.), holds that mere knowledge of the performance of work and furnishing of materials is not enough for consent under s. 8(3). It did not

involve a construction mortgage, but Justice Stewart referred to the situation of a construction mortgage in reaching her conclusion.

[32] Justice Stewart provided an extensive review on the meaning of consent. She said the jurisprudence is "sparse" (para. 29). She held that mere knowledge of the work and materials is not enough (para. 35). At that paragraph, she emphasized the point about mere knowledge by saying:

> …Apart from financing the purchase of the land itself or other projects unrelated to the land, the purpose of a mortgage loan is to fund construction. A mortgage lender would as a condition of making a loan wish to know the purpose for which the monies are to be used. If such knowledge amounts to consent then, in virtually all circumstances, a mortgagee would be deemed to have consented to the additional work. In such a circumstance, the provision of the Mechanics' Lien Act permitting a mortgagee to protect the priority of advances (s. 15(1)) would have no effect. ...

[33] I can expand on Justice Stewart's point. No lender provides construction financing without knowing about the construction. How could a lender finance a construction without at least acquiescing in it?

[34] Justice Freeman said, at para. 27 of the appeal decision in *Glasswall*, "Whether or not the mortgagee has consented is a question of fact." In my opinion, when the mortgagee is financing the construction and the builder works on, and furnishes materials to, the construction the issue is one primarily of law, the application of s. 8(3) in light of s. 15(1).

[35] The requirement in s. 8(3) is not for the lender to consent to the priority of the lien, as was the requirement on the original 1884 statute. The lender need only consent to the performance of the work, or the furnishing of materials. As I say, this could cover almost all construction financings.

[36] The decisions resolving the conflict between s. 8(3) and s. 15(1) conform the statute to the reality of construction financing. This is borne out by the facts of this case.

[37] It was in National Building Group's interests at the beginning of the project that 2M Farms obtain construction financing. The contractor did not contact the bank to get a consent. It contracted the bank for an assurance that financing was in place. The bank gave the required assurance to satisfy the builder, not to subrogate the security for the very financing the builder desired.

[38] The intent in the *Builder's Lien Act* is not to make construction financing impractical. *Northern Electric Co. v. Frank Warkentin Electric Ltd.* and *Northern Electric Co. Ltd. v. Manufacturers Life Insurance* determined that the specific provisions of s. 15(1) about loans advanced after work begins prevail over s. 8(3).

[39] Therefore, the construction mortgage granted to the Royal Bank by 2M Farms Ltd. is not a "prior mortgage" within the meaning of s. 8(3) and the Royal Bank is not within "the mortgagee consents" in s. 8(3)(b).

[40] Thanks to counsel for their professional presentations. I will grant the draft order submitted by the bank when the amount for costs is determined on written submissions or settled by the parties.

J.