THE CLARKSON COMPANY LIMITED, Trustee in Bankruptcy of the Estate of John Ritchie Limited (*Plaintiff*) ..... APPELLANT;

AND

THE CANADIAN BANK OF COMMERCE and GELS GENERAL CONTRACTORS LIMITED (*Defendants*) ..... RESPONDENTS.

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*Mar. 4
Apr. 26

ON APPEAL FROM THE COURT OF APPEAL FOR ONTARIO

Mechanics' liens—Sum of money received by contractor on account of contract price deposited in bank—Appropriation thereof by bank in reduction of contractor's overdraft—Unpaid subcontractors—Payments out of contractor's own funds in fulfilment of contract—Effect of s. 3 of The Mechanics' Lien Act, R.S.O. 1960, c. 233.

The plaintiff as trustee for certain lien claimants brought action against the defendant bank and the defendant construction company for breach of trust. The company was alleged to have received a certain cheque for $31,999.01 as trustee under s. 3(1) of *The Mechanics' Lien Act*, R.S.O. 1960, c. 233, and to have misapplied it by enabling the bank to pay off an overdraft out of the proceeds of this cheque. The trial judgment declared that the sum of $31,999.01 received by the company and deposited to the credit of its account in the defendant bank, or so much thereof as the plaintiff and all others on whose behalf it sues should be found entitled to, constituted a trust fund under s. 3 of *The Mechanics' Lien Act*, directed a reference and judgment against the

*PRESENT: Cartwright, Martland, Judson, Hall and Spence JJ.

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bank for the amount found due on the reference with interest and costs. The judgment provided that the declaration as to the trust fund should be binding on the company but that otherwise the action as against it should be dismissed. On appeal, the Court of Appeal allowed the appeal and dismissed the action.

Held (Judson J. dissenting): The appeal should be allowed, the judgment of the Court of Appeal set aside and the trial judgment restored.

Per Cartwright, Martland, Hall and Spence JJ.: The appeal succeeded on two grounds. Firstly, it having been established that the $31,999.01 came into the possession of the company impressed with the trust created by subs. (1) of s. 3 of *The Mechanics' Lien Act* and that there were unpaid subcontractors who were *prima facie* entitled to the trust fund, the onus of proving the facts, if they existed, which would bring the case within the exception created by subs. (3) lay upon the bank and that onus was not satisfied. Secondly, even if the state of the accounts at the date when the $31,999.01 was received by the company was such that it was entitled under subs. (3) to retain that sum for its own use, its decision whether or not to do so involved the exercise of a discretion vested in it as trustee and the only inference that could reasonably be drawn from the evidence was that it decided to exercise that discretion in favour of the plaintiff and those on whose behalf it sued and not in its own favour.

Per Judson J., *dissenting*: As held by the Court of Appeal, s. 3(3) did not mean retention as part of the trust fund but enabled the contractor, where the conditions of the subsection were met, to use the money for the discharge of his own obligations. The Court of Appeal was right in finding on a review of the facts of the case that subs. (3) applied, that there was no breach of trust in the deposit of this cheque into an overdrawn account and that the bank was entitled to apply it on the overdraft.

[*Passage in Fonthill Lumber Ltd. v. Bank of Montreal*, [1959] O.R. 451 at p. 470, disapproved; *Minneapolis-Honeywell Regulator Co. v. Empire Brass Manufacturing Co.*, [1955] S.C.R. 694, referred to.]

APPEAL from a judgment of the Court of Appeal for Ontario[1], allowing an appeal from a judgment of Gale J., now C.J.H.C., and dismissing an action brought by the appellant as trustee for certain lien claimants. Appeal allowed, Judson J. dissenting.

J. J. Robinette, Q.C., and *D. I. Bristow*, for the plaintiff, appellant.

Hon. R. L. Kellock, Q.C., and *J. W Garrow*, for the defendants, respondents.

The judgment of Cartwright, Martland, Hall and Spence J.J. was delivered by

CARTWRIGHT J.:—This is an appeal from a judgment of the Court of Appeal for Ontario[1] allowing an appeal from a

[1] [1965] 1 O.R. 197, 47 D.L.R. (2d) 289, 6 C.B.R. (N.S.) 312, *sub nom. John Ritchie Ltd. v. Canadian Bank of Commerce et al.*

judgment of Gale J., as he then was, and dismissing the action with costs payable to the respondent the Canadian Bank of Commerce. The judgment of Gale J. declared that a sum of $31,999.01 received by the defendant Gels General Contractors Limited and deposited to the credit of its account in the defendant bank, or so much thereof as the plaintiff and all others on whose behalf it sues should be found entitled to, constituted a trust fund under s. 3 of *The Mechanics Lien Act*, directed a reference and judgment against the bank for the amount found due on the reference with interest and costs. The judgment provided that the declaration as to the trust fund should be binding on the defendant Gels General Contractors Limited but that otherwise the action as against it should be dismissed without costs.

The defendant Gels General Contractors Limited, hereinafter sometimes referred to as "Gels", entered into a contract with the Board of Education for the City of Toronto for the construction of a school. The contract in question is dated November 9, 1959. The contract price was approximately $833,000. Gels entered into subcontracts with various subcontractors for part of the work and material including a subcontract with the plaintiff company covering the plumbing and heating. Work on the main contract commenced about December 1, 1959. As the job progressed part of the work was done by Gels through its own employees and part by the subcontractors through their employees. Some of the materials were obtained by Gels from suppliers with whom it dealt and some were supplied by the subcontractors. Gels paid the wages of its employees when the wages were earned and paid its suppliers as the materials were invoiced without waiting for any progress certificate from the architects. About once a month the subcontractors billed Gels for the value of the work estimated by them to have been done to date and Gels in turn prepared and submitted to the Board through the architects a requisition for payment on account of the contract price, the amount of the payment being calculated by reference to the total value of the work done and material supplied to date and to the total contract price and giving credit for any payments previously made on account. The total value of the work done to the date of

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the requisition included work done and material supplied by Gels through its employees and suppliers. The requisition was checked by the architects and the amount as approved by them, less the statutory holdback of 15 per cent, was paid by the Board to Gels and deposited by Gels in its bank account with the defendant bank. Gels would then issue cheques to the subcontractors for amounts owing by it to them. During the intervals between the submitting of the requisition and the receipt of payment from the Board work on the job continued so that by the time the subcontractors received payment there was an additional amount owing to them by Gels and an additional amount owing to Gels by the Board.

The sum of $31,999.01 in question in this action was paid by the Board on October 27 pursuant to a progress certificate issued by the architects to Gels dated October 13, 1960, following a requisition by Gels dated September 30, 1960. The amount actually approved by the architects was $31,899.01 but by error the cheque was issued for the larger amount. Gels deposited the cheque in its account with the respondent Bank on October 27.

On October 28 Gels issued cheques to the subcontractors including one to the plaintiff for $14,450 but these cheques were dishonoured because the bank applied the whole of the $31,999.01 on an overdraft in the Gels account thereby reducing the overdraft to $6,419.70.

At the date of entering into the contract with the Board Gels had its bank account in the Avenue Road and Dunblaine Branch of the respondent bank in the City of Toronto and it continued to do all its banking there during all relevant times. From November, 1959, to the end of the year 1960, Gels was engaged chiefly on its contract with the Board but it was also engaged on some other building projects. All its receipts from whatever source were deposited in its bank account with the respondent bank and all disbursements were made by cheques drawn on that account including disbursements unconnected with the contract with the Board.

At the time of commencing work on the contract Gels had arranged with the bank for a credit of $45,000. By October, 1960, the bank had decided that it was unwilling to continue to extend credit to Gels and viewed with some

alarm the state of its account. To the knowledge of the branch manager of the bank Gels was being pressed for payment by the subcontractors and mechanics' liens had been filed on July 25 and October 7. In these circumstances the branch manager decided to appropriate the next payment received by Gels from the Board in reduction of Gels' overdraft and not to extend further credit; he did not so advise Livingstone who was the general manager and virtual owner of Gels.

On ample evidence the learned trial judge has found that, at the time it appropriated the $31,999.01 in reduction of the overdraft, the bank, through its branch manager, knew that it was a sum received by Gels on account of the contract price under its contract with the Board and that a number of subcontractors had not been paid for work done and materials supplied on that contract. The contract was finally completed but the plaintiff and other subcontractors have not been paid in full.

The learned trial judge found that on the evidence it was reasonably clear that in the month of October, 1960, between the date of the requisition for payment and the receipt of the $31,999.01 Gels had paid out to its own employees and suppliers amounts totalling more than that sum.

On these findings of fact, the question to be determined was as to the effect of s. 3 of *The Mechanics' Lien Act* which reads as follows:

> 3. (1) All sums received by a builder or contractor or a subcontractor on account of the contract price are and constitute a trust fund in the hands of the builder or contractor, or of the subcontractor, as the case may be, for the benefit of the proprietor, builder or contractor, subcontractors, Workmen's Compensation Board, workmen and persons who have supplied material on account of the contract, and the builder or contractor or the subcontractor, as the case may be, is the trustee of all such sums so received by him, and until all workmen and all persons who have supplied material on the contract and all subcontractors are paid for work done or material supplied on the contract and the Workmen's Compensation Board is paid any assessment with respect thereto, may not appropriate or convert any part thereof to his own use or to any use not authorized by the trust.
>
> (2) Every builder, contractor or subcontractor who appropriates or converts any part of the contract price referred to in subsection (1) to his own use or to any use not authorized by the trust is guilty of an offence and on summary conviction is liable to a fine of not more than $5,000.00 or to imprisonment for a term of not more than two years or both, and every director or officer of a corporation who knowingly assents to or acquiesces

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in any such offence by the corporation is guilty of such offence in addition to the corporation.

(3) Notwithstanding the other provisions of this section, where a builder, contractor or subcontractor has paid in whole or part for any materials supplied on account of the contract, or any workman or subcontractor who has performed any work or services or placed or furnished any material in respect of such contract, the retention by such builder, contractor or subcontractor of any amount so paid by him shall not be deemed an appropriation or conversion thereof to his own use or to any use not authorized by the trust.

The reasons of the learned trial judge make it clear that, had he regarded the question as being *res integra*, he would have construed subs. (3) as modifying the effect of subs. (1) so as to constitute the contractor not only a trustee of all sums received by him on account of the contract price but also a beneficiary under the trust created by the subsection to the extent that he had paid out of his own funds for work done and materials supplied in performance of the contract. The learned judge was however of opinion that he was bound to hold otherwise by the judgment of the Court of Appeal delivered by Schroeder J.A. in *Fonthill Lumber Ltd. v. Bank of Montreal*[1] and particularly the following passage at p. 470:

It was urged that the bank manager might have believed that the contractor had paid out of his own money for the materials supplied on account of the contracts in question or for work performed thereon with the result, that in using the moneys on deposit to pay his indebtedness to the bank he was not to be deemed to be appropriating or converting these moneys by virtue of s. 3(3). Obviously, the fallacy of this argument lies in the fact that he was thereby divesting himself of the money, and s. 3(3) only prevents the retention thereof by the builder from operating as a wrongful appropriation or conversion within the meaning of that section.

The Court of Appeal regarded the passage just quoted as *obiter dictum* and disagreed with it. Roach J.A. who delivered the unanimous judgment of the Court said in part:

By virtue of s. 3(1) the sums which are the subject of the trust thereby created are any sums 'received by a builder or contractor or a subcontractor on account of the contract price'. When, as in this case, an owner makes an interim payment to a general contractor pursuant to a progress certificate it is made on account of the whole contract price. The certificate on the strength of which the Board paid the $31,999.01 states in terms that Gels 'is entitled to a payment of $31,899.01 being tenth: Payment on the contract'.

Who are the beneficiaries of that trust? It is plain from subs. (1) that they are and were thereby intended to be all those persons who contributed to the totality of the work and material up to the date of payment. Included among them, in the instant case, was Gels which had contributed to that totality through its own workmen and material men.

[1][1959] O.R. 451.

Gels was therefore both a trustee of the $31,999.01 received by it and one of the beneficiaries of that trust. Subsection (1) standing by itself prohibited Gels from appropriating or converting any part of that trust fund to its own use or to any use not authorized by the trust until, among others, all subcontractors had been paid. By reason of that prohibition a subcontractor would have a preferential right to payment out of the trust fund to compensate him not only for any moneys expended by him but also for his earned profit before Gels, as the general contractor, could have recourse to the fund to compensate itself even for moneys expended by it for labour or material that had gone into the building.

In 1952 the Legislature amended s. 3 by adding thereto subss. (2) and (3). In my opinion on the plain wording of subs. (3) Gels as the contractor was entitled to retain out of the trust fund sufficient to recoup itself for moneys that it had paid to its employees, workmen, material men or subcontractors. The word 'retention' as used in subsection (3) cannot mean retention as part of the trust fund. The 'retention' thereby authorized is a retention which, were it not for subs. (3), would amount to a prohibited appropriation or conversion by the contractor to his own use and a retention in the trust fund obviously would not amount to such an appropriation or conversion. The contractor is still not put on an equal footing with the subcontractor. The former has only the right to recoup itself out of the trust fund for moneys actually expended out of its own pocket for labour or material or in payments to subcontractors; the latter's beneficial interest in the trust fund includes not only any amount expended out of its pocket for that purpose but also its earned profit.

There is nothing in the whole of s. 3 amounting to a direction as to the manner in which the trust fund created by subs. (1) is to be apportioned among those entitled and in the absence of such a direction it has been held by Rand, J. in *Minneapolis-Honeywell Regulator Co. Limited v. Empire Brass Manufacturing Co. Limited* [1955] S.C.R. 694 at 697 that the trustee has a discretionary power and his obligation is satisfied when the trust moneys are paid out to persons entitled whatever the division. Certainly so long as the trust fund was used for a trust purpose the position of the bank would not be affected whether or not Gels unduly preferred itself in retaining out of the trust fund sufficient to recoup itself to the detriment of other beneficiaries.

This passage, in my opinion, correctly interprets s. 3. It appears to have been the view which the learned trial judge would have adopted had he felt free to do so.

After discussing the *Fonthill* case Roach J.A. concluded his reasons as follows:

When the $31,999.01 came into the hands of Gels it did constitute a trust fund but for the reasons stated Gels was entitled to retain it for its own use by way of recoupment for moneys expended out of its own pocket for labour and material that had gone into the job and for payments made to subcontractors without thereby committing a breach of the trust. This it did by putting that money within the reach of the bank which, as it was entitled to do, applied it on Gels' indebtedness. That indebtedness had been incurred in the first place when the bank advanced moneys to Gels so that Gels could thus expend it.

The appeal should be allowed with costs and the action dismissed with costs.

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With respect, it appears to me that in the first sentence of this passage Roach J.A. overlooked an aspect of the matter to which the learned trial judge had called attention. After considering the argument of counsel for the bank that there had been no breach of trust on the part of Gels because it had expended out of its own funds in fulfilment of the contract during the month of October more than $31,999.01, Gale J. continued:

> Had the argument on behalf of the Bank on this point succeeded, it would not have meant necessarily that the action would be dismissed. I say that for this reason: the trust could only be discharged to the extent that all payments made by Gels out of its own funds exceeded any monies retained by it from draws. In other words, to make subsection (3) effective, it would have to be shown that the total of all monies paid out by Gels on the contract prior to October 27 was at least $31,999.01 greater than the total of draws received by it prior to that date, and the fact that Gels expended more in October that it received in that month would not automatically give it the right to keep the whole of the $31,999.01.
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> I also venture to add that had I been obliged to consider this last point, I would have been inclined to the view, having regard to *Pleet v. Canadian Northern Quebec R.W. Co.*, 50 O.L.R.223, affirmed [1923] 4 D.L.R. 1112, that the onus of establishing that the whole or any part of the $31,999.01 was released from the trust would rest upon the Bank.

I am in agreement with the first paragraph of this passage. It will be necessary to consider the second paragraph later.

In answer to questions from the bench counsel for the appellant and for the respondent stated that it is not possible to determine from the evidence in the record whether, as of October 27, 1960, the total of all payments made by Gels out of its own funds in fulfilment of the contract exceeded the total moneys retained by it out of sums received by it on account of the contract price.

In this state of affairs it would at first appear that judgment must go against the party on whom lay the onus of proving the matters of fact referred to in the preceding paragraph. For the appellant it was contended that the onus lay upon the bank not only for the reason indicated by the learned trial judge in the second paragraph of the passage last quoted above but also because it was established that the bank had appropriated in discharge of Gels' personal liability to it moneys which it knew that Gels had received in trust. The appellant argues that the fact that under certain circumstances Gels might also turn out to be a beneficiary of the trust was not sufficient to place on the

plaintiff the onus of proving that Gels was not beneficially entitled to the trust fund.

For the respondent bank it is argued that the plaintiff having alleged a breach of trust the onus of shewing that Gels was not entitled as beneficiary lay upon the plaintiff because until that was shewn there was no proof that a breach of trust had been committed.

I have reached the conclusion that in the circumstances of this case the onus lay upon the respondent bank to shew that Gels was entitled as beneficiary to all or part of the $31,999.01, and that it has not discharged that onus.

In determining what result flows from this it is necessary to consider the course of the proceedings at the trial. Before any evidence was called an agreement as to certain facts was filed. It concludes with the following paragraph:

> 8. Should it be held that the sum of $31,999.01 is subject to a trust and there was any breach of trust with respect thereto to which the bank was a party and a reference is directed, the parties shall be free to adduce such evidence as they see fit as to the amount of the payment of $31,999.01 discharged from the trust and the amounts of the claims of the plaintiff and other subcontractors on whose behalf this action has been brought thereagainst.

It does not appear to me that the wording of this paragraph relieved either party from the necessity of leading such evidence as was necessary to prove or disprove that (i) the sum of $31,999.01 or part thereof, was subject to a trust, (ii) that there was a breach of that trust, and (iii) that the bank was a party to the breach. Unless each of these three matters were found the action would fail and there would be no occasion for a reference.

On the evidence in the record and the findings of the learned trial judge it is established that Gels received the $31,999.01 impressed with the trust created by s. 3 of *The Mechanics' Lien Act,* that the claims of several beneficiaries under that trust remained unpaid and that the bank with knowledge of these facts applied the sum in question in reduction of the personal liability of Gels to it. If the matter rested there it would appear that the appeal should be allowed and the judgment at trial restored. It does however appear from the record that Gels paid substantial sums to subcontractors out of its own funds. As already pointed out, there is no way of determining from the record as it stands whether or not the total of the sums so paid by

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Gels for work done and materials supplied in performance of the contract exceeded the total of all payments received by it on account of the contract price. The judgment at the trial directs a reference in the following terms:

> 4. AND THIS COURT DOTH FURTHER DIRECT a reference to the Master of the Supreme Court of Ontario to ascertain which of the plaintiff and all others on whose behalf it sues under Section 3 of the *Mechanics' Lien Act*, are to participate in the said fund, and their respective degrees of participation, the parties to be free to adduce upon such reference such evidence as they see fit as to the amount of the said sum of $31,999.01, subsequently discharged from the trust and the amount of the claims of the plaintiff and all others on whose behalf it sued thereagainst.

It would not appear that on the reference so directed the bank could give evidence to shew that Gels was beneficially entitled to all or part of the sum of $31,999.01; the judgment decides the contrary. While the judgment was founded primarily on the view of the law propounded in the passage from the judgment in the *Fonthill* case, quoted above, which has now been rejected, the learned trial judge also indicated his inclination to the view that the onus of proving that Gels was beneficially entitled to all or any part of the sum in question lay upon the bank and had not been discharged. I have already expressed my agreement with this view.

In the circumstances it appears to me that the proper course is to allow the appeal and restore the judgment at the trial.

I wish, however, to rest my judgment also on another ground put forward by counsel for the appellant. Assuming, for the purposes of this branch of the matter, that in fact when Gels deposited the cheque for $31,999.01 the total of all payments made by it out of its own funds in fulfilment of the contract exceeded by that amount the total of all payments received by it on account of the contract price, the result would not be that the $31,999.01 was not subject to the statutory trust created by s. 3; it would be, as pointed out by Roach J.A., that Gels was trustee of the fund and also one of the beneficiaries of the trust. In *Minneapolis-Honeywell Regulator Co. Ltd. v. Empire Brass Manufacturing Co. Ltd.*[1], Rand J. was speaking for the majority of the Court when he held that s. 19 of the *Mechanics' Lien Act* of British Columbia, which is indistinguishable from s. 3(1) of the Ontario Act, did not re-

[1] [1955] S.C.R. 694.

quire the statutory trustee (in that case a subcontractor) to make a *pro rata* distribution among the beneficiaries. His actual words at p.697 were:

> Section 19 does not, however, require that they be distributed on a *pro rata* basis. The subcontractor has, in this respect, a discretionary power, and his obligation is satisfied when the trust moneys are paid out to persons entitled, whatever the division. This, of course, might be affected by rights of unpaid trust creditors under other provisions of law.

This pronouncement appears to treat the trust created by the statute as an exception to the general rule that a trustee must hold an even hand between the beneficiaries and not benefit one at the expense of the others but, accepting it as stating the rule applicable to this trust, the situation is as follows. When Gels received the $31,999.01 it did so as trustee but had a discretionary power to pay it to one or more of the beneficiaries to the exclusion of the others. It had therefore, in the assumed situation, a discretion to retain it all for itself. Gels acted throughout by its general manager Livingstone and it appears to me that the only reasonable inference to be drawn from the relevant evidence is that Livingstone decided not to retain the money for Gels but to pay it out to the plaintiff and the others on whose behalf the plaintiff sues. It is elementary that a trustee cannot delegate the exercise of a discretion committed to him by the instrument creating the trust and *a fortiori* he cannot be compelled by a creditor who is a stranger to the trust to exercise his discretion in a particular manner which will benefit that stranger to the detriment of the beneficiaries.

We are not here concerned with any question which would arise if the bank without knowledge of the existence of the trust had acquired legal title to the trust fund. The findings that the branch manager was fully aware of the existence of the trust and of the intention of Gels to distribute the fund among the beneficiaries other than itself cannot be successfully challenged.

For these reasons I have reached the conclusion that even if the state of the accounts, which was not proved, was such that Gels had the right to retain the $31,999.01 this circumstance would not assist the respondent; Gels did not elect to exercise the right of retention. Gels' relationship to the bank was that of a debtor to its creditor; its

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relationship to the plaintiff and those on whose behalf it sues was a dual one, that of a debtor to its creditors and that of a trustee to the beneficiaries of the trust. It chose to exercise its discretion in favour of the beneficiaries; the bank had no standing to require it to alter that choice. On this view it does not matter whether the state of the accounts in connection with the contract was such that Gels would have had the right to retain the fund in question for its own use had it seen fit to do so.

With respect, I think that Roach J.A. was in error when he said, at the conclusion of his reasons in the passage quoted above, that Gels by putting the money within the reach of the bank was evidencing an intention to retain it for its own use. The evidence is to the contrary. Livingstone's intention, which in the circumstances was the intention of Gels, was to follow an established practice of depositing the trust moneys in Gel's only bank account and paying it out forthwith to its subcontractors who were beneficiaries of the trust; that this was his intention was well known to the branch manager of the bank.

To summarize, it is my opinion that the appeal succeeds on two grounds. Firstly, it having been established that the $31,999.01 came into the possession of Gels impressed with the trust created by subs. (1) of s. 3 of *The Mechanics' Lien Act* and that there were unpaid subcontractors who were *prima facie* entitled to the trust fund, the onus of proving the facts, if they existed, which would bring the case within the exception created by subs. (3) lay upon the bank and that onus was not satisfied. Secondly, even if the state of the accounts at the date when the $31,999.01 was received by Gels was such that it was entitled under subs. (3) to retain that sum for its own use, its decision whether or not to do so involved the exercise of a discretion vested in it as trustee and the only inference that can reasonably be drawn from the evidence is that it decided to exercise that discretion in favour of the plaintiff and those on whose behalf it sues and not in its own favour.

I would allow the appeal, set aside the judgment of the Court of Appeal and restore the judgment of the learned trial judge. The appellant will recover from the respondent bank its costs in the Court of Appeal and in this Court.

JUDSON J. (*dissenting*):—This action was brought by the Clarkson Company Limited as trustee for certain lien claimants against the Canadian Bank of Commerce and Gels General Contractors Limited for breach of trust. The contractor was alleged to have received a certain cheque for $31,999.01 as trustee under s. 3(1) of *The Mechanics' Lien Act* and to have misapplied it by enabling the bank to pay off an overdraft out of the proceeds of this cheque. The Court of Appeal held that the case fell within s. 3(3) of *The Mechanics' Lien Act* and that there was no breach of trust. In so finding they disapproved of the dictum in *Fonthill Lumber Limited v. Bank of Montreal*[1]. That dictum had said that the right given by s. 3(3) was merely a right of retention. The Court of Appeal held that it did not mean retention as part of the trust fund but enabled the contractor, where the conditions of subs. (3) were met, to use the money for the discharge of his own obligations.

I agree with this interpretation of subs. (3). It is clear that the learned trial judge would himself have placed the same interpretation on the subsection had he not considered himself bound by the decision in *Fonthill*. It has to be remembered that the *ratio* of the trial decision in this case was that there was a breach of trust because subs. (3) did not authorize more than a retention.

Now the argument is submitted to us that there was a breach of trust unless the third party, the bank that received the money, can show by going through every draw on the contract (and it should be noted that this was the tenth draw) that the job owed the construction company at least $31,999.01 more than the total of the draws. Each side on the appeal admitted that the case had not been presented in such a way as to make this possible. The appellant says that the onus was on the bank to do this. With this I do not agree. The plaintiff, in instituting this action, undertook the burden when he sued a third party of proving a trust and proving knowing participation in the breach of trust, and I think that the Court of Appeal was right in finding on a review of the facts of the case that subs. (3) applied, that there was no breach of trust, that the construction company was entitled to apply the cheque in payment of its overdraft, and that the bank was entitled to receive this payment.

[1] [1959] O.R. 451.

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The facts are set out in great detail in the reasons at trial[1] and summarized in the reasons of the Court of Appeal[2]. All that I need to say is that they show that the construction company was borrowing from the bank from month to month for the purpose of paying accounts for the job, that when the time approached for another draw it was heavily in debt to the bank, that whenever it deposited a cheque for the draw it cleared off the existing indebtedness as far as the cheque would go and then began to borrow again to pay off more debts. It was always behind because the owner never did or could pay everything owing up to the date of the cheque. For example, the cheque for $31,999.01 in question in this action was dated October 27, 1960 and was issued pursuant to a progress certificate from the architects dated October 13, 1960, which, in turn, was based upon a requisition issued by the construction company dated September 30, 1960.

I have no doubt that when the construction company deposited this cheque it expected to go on as before. It issued cheques on October 28 payable to subcontractors. These were dishonoured because the bank appropriated the whole of the cheque, which reduced the overdraft to $6,417.70, and then refused to honour further cheques. It is clear that the bank had given no undertaking that it would continue to honour cheques for which there were no funds and that the construction company when it made the deposit had not attempted to impose any conditions that further cheques would be honoured.

In these circumstances and with the rejection of the interpretation given to subs. (3) in the *Fonthill* case, I am in full agreement with the reasons of Roach J.A. in the Court of Appeal that there was no breach of trust in the deposit of this cheque into an overdrawn account and that the bank was entitled to apply it on the overdraft.

I would dismiss the appeal with costs.

Appeal allowed with costs, JUDSON J. *dissenting.*

Solicitors for the plaintiff, appellant: Timmins and Bristow, Toronto.

Solicitors for the defendants, respondents: Blake, Cassells & Graydon, Toronto.

[1] [1963] 2 O.R. 116, 38 D.L.R. (2d) 546.
[2] [1965] 1 O.R. 197, 47 D.L.R. (2d) 289, 6 C.B.R. (N.S.) 312.