Canadian College of Construction Lawyers

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INSIDE THIS ISSUE:

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

LUC #146 [2018]

Primary Topic:
I General
Jurisdiction:
Quebec
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The following article discusses a decision of the Quebec Court of Appeal in the case of a major group of construction companies which ran afoul of the recent Quebec inquiry, known as the *Charbonneau Commission*, into corruption and fraudulent practices in public contracting in the construction industry in Quebec. The subject was discussed by Mr. Justice François Rolland during the Quebec City conference of the College. The article was published in *Construction Law Reports*, 66 C.L.R. (4th) 31 and is reproduced in this Legal Update report with the kind permission of Carswell.

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

Arrangement relative à Investissements Hexagone inc., 2017 QCCA 970

The ripple effect of a highly anticipated decision of the Quebec Court of Appeal in the matter of a powerful group of construction companies which ran afoul of the recent Quebec inquiry into corruption and fraudulent practices in public contracting in the construction industry in Quebec, known as the *Charbonneau Commission*, deserves our attention. The judgment is styled *Arrangement relative à Investissements Hexagone inc.*, 2017 QCCA 970). It deals with the repercussions of new legislation upon innocent sureties who, prior to the promulgation of the new legislation, had issued labour and materials payment bonds on behalf of corrupt contractors and upon innocent subcontractors who believed they were creditors under such bonds.

The many companies in the Hexagone group[1] were linked directly or indirectly at some point to one Antonio Acurso, whose name figured prominently and ignominiously in hearings of the *Charbonneau Commission*. Upon the heels of the report of the *Charbonneau Commission*, the Quebec legislature enacted Bill 26 - *An Act to ensure mainly the recovery of amounts improperly paid as a result of fraud or fraudulent tactics in connection with public contracts* – to censure the many contractors and major engineering firms named in the hearings of the *Charbonneau Commission* and to compel them to disgorge the illicit profits they were deemed to have made.

This new law, undoubtedly a political and societal response to the damning conclusions of the *Charbonneau Commission*, focused primarily on the reimbursement of sums improperly paid by public bodies to contractors and engineers as a result of fraud or corruption. The law reversed the burden of

[1] Investissements Hexagone inc., Location Hexagone inc., Groupe Hexagone, s.e.c., Les Entreprises commerciales Hexagone inc., 9324-9928 Québec inc., 9328-5021 Québec inc. and 9325-0041 Québec inc.

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

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LUC #146 [2018]

Primary Topic:
I General
Jurisdiction:
Quebec
Author:
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De Grandpré Chait

QUEBEC

proof by placing the onus on the suspect entities to exculpate themselves, subjected suspect entities to a presumed obligation to reimburse roughly 20% of monies deemed improperly received unless the suspect entities voluntary reimbursed their ill-gotten gains, extended the prescriptive delays (time limitation) to reach into the past and rendered officers and directors of the suspect companies personally liable for the restitution.

The new law rocked segments of the construction industry (although the shock was predictable), even those who were not directly involved in the fraudulent practices of the corrupt contractors and engineers. The new legislation cast a broad shadow. It raised peripheral issues that impacted upon the innocent. In a motion for leave to appeal and a lead-up to the 2017 decision of the Court of Appeal *a quo* which is at the heart of this commentary, Justice Schrager of the same Court said that "the points in appeal are novel and of significance to the practice. While I do not have hard evidence before me, it is hardly inconceivable that similar situations may arise before the courts from the fallout of the findings of the *Charbonneau Commission* and the application of *Bill 26*. The Applicants have pleaded, without contradiction, that the situation has no precedent" (*Aviva compagnie d'assurances du Canada c. Béton Brunet 2001 inc*., 2016 QCCA 1837, paragraph 9).

A brief recap of the facts is warranted. The Hexagone companies had received important construction contracts over the years from the Cities of Montreal and Laval. To illustrate the order of magnitude of such contracts, the Cities of Montreal and Laval claimed $44,721,825 and $30,000,000 respectively from the Hexagone companies because of contracts awarded to them through corrupt or fraudulently deceptive bidding practices.

With their empire imperilled and painted at large as corrupt by the indiscriminate broad brush of Bill 26, the Hexagone companies sought financial refuge behind the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c C-36. Under the protection of that insolvency legislation, legal proceedings were stayed and the trustee, PricewaterhouseCoopers inc., was appointed to monitor the business and financial affairs of the Hexagone companies. The Hexagone companies justified their invocation of the *CCAA* on the grounds that the Cities of Montreal and Laval owed them substantial sums, which they needed in order to survive and pay their subcontractors. Indeed, about 140 subcontractors of the Hexagone group were unpaid, with claims exceeding $25,00,000. The quandary facing the Hexagone companies lay with the refusal of the Cities of Montreal and Laval to pay the amounts the Cities otherwise owed to the Hexagone companies on the grounds that these Cities were entitled to recover from the Hexagone companies the pro-

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LUC #146 [2018]

Primary Topic:
I General
Jurisdiction:
Quebec
Author:
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De Grandpré Chait

QUEBEC

ceeds of corruption and to set-off their overwhelming claims against the significant yet inferior claims of the same Hexagone companies.

Given this background, the unpaid subcontractors of the Hexagone companies were loath to rely entirely upon complicated and protracted machinations under the *CCAA* to recover the amounts owed to them, or some fraction thereof, by the Hexagone companies. So the unpaid subcontractors brought proceedings against Aviva Compagnie d'assurance du Canada and Zurich Compagnie d'assurances SA under outstanding payment bonds for labour, material and services that had been issued by these sureties in respect to bonded Hexagone projects in order to be paid under the bonds.

The subcontractors' strategy was concisely summarized and correctly understood by the Hon. Justice Schrager of the Court of Appeal in the precursor motion to leave (*Aviva compagnie d'assurances du Canada c. Béton Brunet 2001 inc*., previously cited) who said: "[15] The quantum of indebtedness of the debtors [the Hexagone companies] in the *CCAA* files may not ultimately be altered because the insurance companies, when and if they pay, may assert claims by way of subrogation [against the bonded Hexagone companies]. However, the sub-contractors will potentially obtain *quick and substantial payments* if the judgment of first instance is confirmed. There are a large number of sub-contractors potentially affected in addition to Respondents."(Parenthesis and emphasis added.)

The Superior Court issued a provisional safeguard order so that neither Aviva or Zurich had to release any sums to bonded subcontractors pending resolution of certain legal issues. The subcontractors appointed a representative under the *Companies' Creditors Arrangement Act*, who launched proceedings seeking a declaratory judgment from the Superior Court to define the rights of the bonded subcontractors under against the sureties, Aviva and Zurich.

The trial judge ruled that the failure of the Cities of Montreal and Laval - not being parties to the payment bonds - to pay the Hexagone companies under the construction contracts did not release Aviva and Zurich from their obligations to pay the bonded subcontractors, subject to the subcontractors complying with the formalities under the bonds for presenting and proving their claims.

Aviva and Zurich appealed on two grounds. The first ground reasoned that the Cities of Montreal and Laval effectively were 'parties' to the payment bonds and the surety, in the shoes of the Hexagone companies, did not have to honour its payment obligations to the subcontractors since the Cities, being 'parties' to the bonds, were in default thereunder to pay the Hex-

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

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LUC #146 [2018]

Primary Topic:
I General
Jurisdiction:
Quebec
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De Grandpré Chait

QUEBEC

agone companies. The second ground advanced by Aviva and Zurich relied on the principle that suretyship may not be extended beyond the limits for which it was contracted (Article 2343 of the *Civil Code of Quebec*) – that is, suretyship cannot be rendered more onerous than originally contemplated, which materialized when unforeseen restitution legislation gave the Cities of Montreal and Laval a fresh excuse for withholding payments from the Hexagone companies.

The Court of Appeal paused to underscore the purpose of payment bonds in public projects, which is to provide a subcontractor with a payment guarantee in the absence of a subcontractor's right to a construction hypothec (lien) against the public domain. Requiring payment bonds in public projects encourages the participation of subcontractors in public projects at reasonable costs. Construction bonding is a legislative requirement for public contracting in the construction industry in Quebec under *Règlement sur les contrats de travaux de construction des organismes publics*, RLRQ, c. C-65.1, r. 5, although this Regulation does not apply to the Cities of Montreal and Laval. Nevertheless, both Cities generally and systemically require bidders to arrange for construction bonding as an essential tender prerequisite.

In that context, the Court of Appeal held that the issue of whether or not the Cities of Montreal and Laval were 'parties' to the payment bonds was not a determining factor since the obligations of Aviva and Zurich to pay the subcontractors was unambiguous, given the wording of the payment bonds, Aviva and Zurich having accepted the full risk of paying the bonded subcontractors regardless of the refusal of the Cities of Montreal and Laval to pay the Hexagone companies because of the new corruption restitution legislation.

Aviva and Zurich also argued that the Cities of Montreal and Laval indirectly were 'parties' to the payment bonds in the sense that such bonds were stipulations for the benefit of a third party (namely, for the benefit of the two Cities). As such and since the Cities were 'parties' both to the payment bonds as well as to the construction contracts linked to the corresponding payments bonds *at the same time*, the default of the Cities to respect their obligation to pay the Hexagone companies under the construction contracts released the sureties from their obligations to pay the subcontractors under their payment bonds. They sought to invoke Article 1450 of the Civil Code of Quebec which provides that:

> 1450. A promisor may set up against the third person beneficiary such defenses as he could have set up against the stipulator.

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

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LUC #146 [2018]

Primary Topic:
I General
Jurisdiction:
Quebec
Author:
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De Grandpré Chait

QUEBEC

[Although not mentioned in the judgment, the mechanism of the standard bonding relationship looms in the background. Upon application of a contractor, a surety agrees to compensate unpaid subcontractors who provide labour, materials and services in respect of a particular bonded project should the contractor default to do so. By virtue of other contractual arrangements, the contractor assigns the amounts owing to him by an owner or awarding authority under the bonded construction contract. If the surety pays bonded subcontractors, the surety is subrogated in the subcontractors' rights against the contractor to the extent of the payments made to the subcontractors and can recover under the assignment all or part of the contract price which the owner or awarding authority owes to the bonded contractor.]

The Court of Appeal did not accept the contentions of Aviva and Zurich. The Court held that Cities of Montreal and Laval, regardless of whether or not they were 'parties' to the payment bonds, had assumed in unambiguous terms the obligation of paying the subcontractors regardless of the nature or cause of the risk which impelled the Cities not the pay the Hexagone companies. In effect, said the Court, Aviva and Zurich cannot unilaterally and retroactively add a clause excluding their liability for the unforeseen restitution risk confronting the Hexagone companies as a result of new legislation introduced after the payment bonds had been issued – which would compromise the fundamental purpose of such bonds.

Nor would a right of compensation (or 'set-off') apply since the Cities of Montreal and Laval and the Hexagone companies were not bound directly together by a single synallagmatic contract that created simultaneous, related, balanced and reciprocal obligations on both sides. There is no correlation between a contractor's payment obligation to his subcontractor, arising from a construction subcontract, and a surety's obligations to pay bonded subcontractors, arising from the payment bonds. The foregoing arguments apply even if the payment bonds are characterized as being unilateral stipulations of a surety for the benefit of third parties (namely, the Cities).

Aviva and Zurich further argued that that the risk to the Hexagone companies under the new corruption restitution legislation did not exist at the time the payment bonds were issued. The new legislation therefore represented an unforeseeable risk which Aviva and Zurich never assumed, thereby infringing the prohibition in Article 2343 of the *Civil Code of Quebec* to render a contract of suretyship more onerous than originally contracted:

> **2343.** Suretyship may not be extended beyond the limits for which it was contracted.

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

LUC #146 [2018]

Primary Topic:
I General
Jurisdiction:
Quebec
Author:
David H. Kauffman,
De Grandpré Chait

QUEBEC

Repercussions of Quebec Corruption Restitution Legislation on Sureties and Subcontractors

Aviva and Zurich invoked common law principles along the same lines as Article 2343 of the Quebec Civil Code. The Court of Appeal did not these arguments of Aviva and Zurich. The Court held that the payment bond secured payment of the price in the subcontract, which it identified as being the 'principal contract' under a payment bond; thus a modification affecting the construction contract between an owner and the general contractor would not constitute a change affecting the 'principal contract' - the subcontract - and rendering it more onerous. The Court cited Dickson J. in *Truro (Town) v. Toronto General Insurance Co.,* [1974] SCR 1129, a decision under the common law of Ontario, at pages 1140 and 1141:

> The bond is conditioned for the due payment by Kenney [the contractor] of all claimants for all labour and material used or reasonably required for use in the performance of the prime contract. The town [the awarding owner] is named as trustee for all potential claimants and referred to as the obligee. *The contracts, performance of which is guaranteed by the surety, are the subcontracts entered into by Kenney with labourers and materialmen*. A "Claimant", for the purposes of the bond, is defined as one having a direct contract with Kenney for labour, material or both, used or reasonably required for use in the performance of the prime contract. In the present instance Arthur & Conn Ltd. is such a claimant. *The contract, performance of which is guaranteed, is the subcontract between Kenney and Arthur & Conn Ltd. dated August 4, 1969*. The town is not a party to that contract. Nothing done by the town made any change in or alteration to that contract. It is submitted on behalf of the surety, however, that regard must be had also to the prime contract because the prime contract is by reference made a part of the bond and the surety is discharged if there has been any material change in the prime contract. *For myself, I do not think that can be so*. The plain words of the bond do not support the submission. The "NOTE" at the top of the bond makes evident that "another bond" is conditioned for the due performance of the prime contract. *In* Doe et al. v. Canadian Surety Co.*[1936 CanLII 9 (SCC), [1937] R.C.S. 1] and in each of the other cases cited to this Court, the acts of the obligee relate to the contract, performance of which is guaranteed by the surety. The Court has not been referred to any case, and I can find none, in which a material change in contract A, to which the obligee is a party, discharged a guarantee in respect of contract B, to which the obligee is not a party.*
>
> [In the Judgment, the above passage is in French. The English version istaken from the Supreme Court Re-

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I General
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De Grandpré Chait

QUEBEC

ports, with the same added underlining as in the instant decision of the Court of Appeal.]

In the eyes of the Court of Appeal, whether under the civil law of Quebec or under Canadian common law, the approach of Aviva and Zurich is not sustainable. In the absence of a clear provision in the payment bond, a surety cannot escape its obligations to pay a bonded subcontractor by invoking a default of the owner/awarding authority under the construction contract entered into with the general contractor.

In the eyes of the writer of this commentary, a surety's refusal to pay because of the introduction of new legislation is no more than a stratagem not to pay. Had Quebec not enacted legislation allowing for the recovery of profits illicitly gained, an owner nonetheless might decline, rightly or wrongly, to pay a bonded contractor who has engaged in corrupt or fraudulent practices to the prejudice of the owner. And, in such circumstances, bonded subcontractors would still retain their rights against a surety under a labour and materials payment bond and, conversely, a surety would have to respect his obligations to a bonded subcontractor under the payment guarantee which the surety assured.

Consolidated Contractors Group S.A.L. (Offshore) v. Ambatovy Minerals S.A., 2017 ONCA 939

LUC #146 [2018]

Primary Topic:
XIV Mediation and Arbitration
Jurisdiction:
Ontario
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CanLII References:

Court of Appeal

ONTARIO

Court of Appeal Rejects Challenge to International Commercial Arbitral Award

On December 4, 2017 the Ontario Court of Appeal dismissed an appeal from the judgment of Justice Penny, 2016 ONSC 7171, upholding an international commercial arbitral award. The decision affirms given the relatively narrow grounds for judicial intervention provided for in the UNCITRAL Model Law. This decision is of interest for the Court's thorough analysis of the grounds for judicial intervention under the Model Law, and in particular for its examination of the issue of compliance with contractual pre-arbitration dispute resolution steps. The latter issue is a common problem as many construction contracts provide for staged or escalated dispute resolution processes as a precursor to arbitration, often expressed in mandatory terms. The case also affirms the principle expressed by the Court of Appeal in *Popack v Lipszyc*, 2016 ONCA 135 that "the parties' selection of their forum implies both a preference for the outcome arrived at in that forum and a limited role for judicial oversight of the award made in the arbitral forum".

The dispute concerned the construction of a 220 km slurry pipeline from an inland mine site to a coastal refinery in Madagascar. The prime contract provided for an escalating dispute resolution procedure culminating in arbitration under the ICC Rules and Ontario law. Strathy C.J.O., writing for a unanimous Court, described the tribunal conducting the arbitration as "blue chip.... with expertise in both commercial arbitration and mega-project construction disputes." After a three week hearing conducted in Toronto in mid-2014, the tribunal issued its award on September 30, 2015. The contractor was awarded only 18 days extension against 294 days of incurred delay and, as a result of the application of liquidated damages for delay in favour of the owner, the net award substantially favoured the owner.

The contractor argued the following grounds in seeking to set aside the Award, both in the lower court and in the Court of Appeal:

> (a) alleged errors of jurisdiction in proceeding to hear the owner's environmental counterclaims without compliance with pre-arbitration dispute resolution conditions, and other grounds;
>
> (b) alleged denial of procedural fairness; and,
>
> (c) alleged breach of Ontario public policy.

The Court of Appeal began its analysis by noting that under the Model Law the tribunal is accorded a high degree of deference. Courts in Ontario will not substitute their judgment for the tribunal's.

With respect to the jurisdictional challenge, the court found that at various points leading up to the arbitration hearing the two sides had taken contrary positions on whether the counterclaims should proceed directly to arbitration without having gone through all of the contractual pre-arbitration dispute resolution steps. The contractor argued, on the other hand, that the

Court of Appeal Rejects Challenge to International Commercial Arbitral Award

Consolidated Contractors Group S.A.L. (Offshore) v. Ambatovy Minerals S.A., 2017 ONCA 939

LUC #146 [2018]

Primary Topic:
XIV Mediation and Arbitration
Jurisdiction:
Ontario
Author:
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CanLII References:

Court of Appeal

ONTARIO

tribunal's jurisdiction was purely consensual and that there absent actual consent, there could be no jurisdiction.

This challenge was dismissed on the basis that the environmental counterclaims had been fully pleaded and defended in the arbitration. Evidence was adduced by both parties and there was full argument on the merits of the counterclaims. The counterclaims arose out of the same project delay asserted by the contractor in support of its own claims. It would not have made any sense, and thus could not have been reasonably contemplated by the parties, to have conducted a second arbitration of the counterclaims which arose out of the same issues of project delay. Essentially the tribunal and both levels of court all characterized the process of arbitrating the counterclaims as thorough and fair.

The Court of Appeal also applied the "close connection" principle. Under Canadian common law, an arbitral tribunal's mandate includes everything "closely connected" to the matters subject to arbitration: *Desputeaux c. Éditions Chouette (1987) Inc.*, 2003 SCC 17.

Finally, and in line with the the U.S. Supreme Court decision in *BG Group plc v. Republic of Argentina* 134 S.Ct. 1198 (2014), the court held that the issue of pre-arbitral steps was one of timing of arbitration, not entitlement to arbitration and, as such, was a procedural matter properly decided by the tribunal and entitled to deference by courts.

Had the contractor's error of jurisdiction argument been accepted by the Court of Appeal, this decision would have raised the stakes considerably for parties hoping to embark on arbitration where imperfect compliance has been observed of contractually prescribed pre-arbitration steps. Indeed, parties are nevertheless well advised to be very cautious in dispensing with or declining to follow contractually mandated pre-arbitration steps given that an arbitrator's decision to accept jurisdiction is discretionary and each case will be reviewed on its own facts. Nevertheless, this decision is helpful in dealing with circumstances where the claims being asserted by one party are closely connected to the claims submitted to arbitration by the other party.

The issues of procedural fairness and violation of public policy were analyzed using a similar deferential standard. To interfere with the award on either basis, the reviewing court must find conduct by the tribunal that offends "basic notions of morality and justice". The application judge rejected the contractor's arguments under these headings, including the argument that in depriving it of "tranche payments" for failing to meet contractual milestones and in awarding the owner liquidated damages for delay, the tribunal's award constituted double recovery for the owner. The tribunal found that the tranche payments and liquidated damages were distinct and served different purposes.

Consolidated Contractors Group S.A.L. (Offshore) v. Ambatovy Minerals S.A., 2017 ONCA 939

LUC #146 [2018]

Primary Topic:
XIV Mediation and Arbitration
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Ontario
Author:
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CanLII References:

Court of Appeal

ONTARIO

Court of Appeal Rejects Challenge to International Commercial Arbitral Award

Nevertheless, in dismissing the application, Justice Penny commented that had there been double recovery he may have been inclined to find a violation of public policy. The Court of Appeal was more terse, finding that the Tribunal's award did not "come close to meeting the test" for violation of public policy which requires a finding of conduct by a tribunal "which offends our local principles of justice in a fundamental way". The Court of Appeal found that the application judge had applied the right test and reached the right result, and therefore declined to comment further on whether a finding of double recovery would have violated public policy.

The application judge had also considered whether he would have upheld the tribunal's decision anyway, even if public policy was violated by awarding damages on the counterclaim that amounted to double recovery. He answered this question affirmatively. However, his finding on this "ultimate discretion" may be of limited precedential value; the Court of Appeal characterized this part of the judgment as *obiter dicta* and stated that it need not deal with the argument. The Court of Appeal confirmed, however, that its decision in *Popack v. Lipszyc* is the governing authority in Ontario in determining whether a reviewing court should exercise its discretion under section 34(2) of the Model Law by declining to set aside an international arbitral award even where grounds exist to do so.

CCG v. Ambatovy confirms that under the Model Law, an appellate court is to approach the tribunal's reasons with considerable deference. Nothing in this decision will provide future unsuccessful parties with much hope that an appeal in Ontario from an international arbitral tribunal constituted under the Model Law will be likely to succeed. However, the decision is recent enough that the time to seek leave to appeal to the Supreme Court of Canada is not yet expired. As of press time it is unknown whether an application for leave will be pursued.

Canotech Consultants Ltd v. 599431 Manitoba Ltd., 2017 MBCA 48

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Manitoba
Author:
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CanLII References:

Court of Appeal

MANITOBA

Reconciling the Definition of Substantial Performance with the Requirement for Certificate of Substantial Performance in Sections 2(1) and 43(1) of The Builders' Liens Act, C.C.S.M. c. B91

Pursuant to subsection 43(1) of the Manitoba Builders' Liens Act[1], a claim for a lien by a contractor may be registered:

- before the performance of the contract;
- during the performance of the contract;
- within 40 days after substantial performance of the contract; or
- within 40 days after abandonment of the contract.

Section 43(1) states:

Time within which claim may be registered by contractor

43(1) Except as provided in section 44[2] a claim for lien by a contractor may be registered before or during the performance of the contract or within 40 days after the substantial performance or abandonment of the contract, as the case may be.

Pursuant to subsection 43(6) of the Act, for the purpose of section 43, substantial performance means the date on which a certificate of substantial performance is given to the owner under section 25[3] or 46[4].

Section 43(6) states:

Meaning of substantial performance

43(6) For the purposes of this section, substantial performance of a contract or a sub-contract means the date on which a certificate of substantial performance thereof is given to the owner under section 25 or 46, as the case may be.

Pursuant to subsection 2(1) of the Act, a contract or sub-contract shall be conclusively deemed substantially performed when certain conditions have been met.

Subsection 2(1) states:

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[1] Subsections (2), (3), (4) and (5) use similar wording in respect of liens by subcontractors, materials, services, and wages

[2] Section 44 applies to liens after substantial performance

[3] When holdbacks may be reduced

[4] Certificate of Substantial Performance by Payment Certifier

Canotech Consultants Ltd v. 599431 Manitoba Ltd., 2017 MBCA 48

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MANITOBA

Reconciling the Definition of Substantial Performance with the Requirement for Certificate of Substantial Performance in Sections 2(1) and 43(1) of The Builders' Liens Act, C.C.S.M. c. B91

Substantial performance

2(1) For the purposes of this Act, a contract or sub-contract shall be conclusively deemed to be substantially performed when

(a) the structure to be constructed under the contract or sub-contract or a substantial part thereof is ready for use or is being used for the purpose intended or, where the contract or sub-contract relates solely to improving land, the improved land or a substantial part thereof is ready for use or is being used for the purpose intended; and

(b) the work to be done under the contract or sub-contract is capable of completion or correction at a cost of not more than

(i) 3% of the first $250,000. Of the contract price,

(ii) 2% of the next $250,000. Of the contract price, and

(iii) 1% of the balance of the contract price.

How does one reconcile subsection 2(1) of the Act with section 43(1)?

This issue was addressed by the Manitoba Court of Appeal in *Canotech Consultants Ltd v. 599431 Manitoba Ltd.*, 2017 MBCA 48.

The facts of Canotech are as follows:

- In July 2010, plaintiff and defendant entered into a Standard Construction Management Contract (the "Contract");
- The project was largely completed December 14, 2011, with December 24, 2011 being the last date plaintiff was at the project;
- There remained a number of deficiencies to be remedied and services performed, including electrical work and other work to be done on the air conditioning system;
- During course of construction, the defendant became dissatisfied with the work being performed. On January 24, 2012, defendant's President directed the plaintiff, via email, to ensure that all trade persons make arrangements with him to do any work on the project as he wanted to supervise the work;
- In February 2012, an electrical company hired by defendant performed work which was finished February 29, 2012. On that date, the electrical company forwarded an email to plaintiff describing the work and including an invoice for supplies required to complete the work. Plaintiff re-

Reconciling the Definition of Substantial Performance with the Requirement for Certificate of Substantial Performance in Sections 2(1) and 43(1) of The Builders' Liens Act, C.C.S.M. c. B91

Canotech Consultants Ltd v. 599431 Manitoba Ltd., 2017 MBCA 48

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Manitoba
Author:
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CanLII References:

Court of Appeal

MANITOBA

viewed that email the same day;

- On March 7, 2012, plaintiff registered a lien; and
- The defendant then filed a motion requesting that the lien be removed on the basis that it was outside the 40-day period. The plaintiff filed a motion seeking a declaration that the lien was valid.

Defendant's Argument

The defendant argued that despite the fact a certificate of substantial performance had not been issued, the time period for registering the lien started to run on December 24, 2011, i.e., the date the contract was substantially performed. The defendant said that on that basis, the plaintiff had until February 2, 2012 to file the lien and since it waited until March 7, 2012 - more than 40 days beyond the period provided for in the Act - the lien was invalid. The defendant relied upon section 2(1) of the Act.

Plaintiff's Argument

The plaintiff argued that irrespective of section 2(1), when section 43(1) is read in conjunction with section 43(6), it is clear that the 40-day period does not start to run until the certificate of substantial performance has been issued. No such certificate was issued.

The Motions Court judge rejected the defendant's argument and granted the plaintiff's motion seeking a declaration that the lien was valid.

In dismissing the owner's appeal and rejecting its argument with respect to substantial performance, Cameron J.A. speaking on behalf of the Court of Appeal, made the following statements:

26 Further, I agree with the plaintiff that, when the Act is read as a whole, the requirement of a certificate of substantial performance to commence the time period set in section 43(1) is consistent with other provisions such as sections 24(1)(a) and 25(1)(a), which require a certificate of substantial performance to be issued in order to engage the time period for determining when holdback monies may be released.

27 Regarding the description of substantial performance found in section 2(1) of the Act, fulfillment of its conditions does not trump the requirement for a certificate of substantial performance in section 43(6). In my view, section 2(1) may be useful as an aid in determining when such a certificate should issue pursuant to sections 46(1) and (2) or when a judge should make an order that a contract has been substantially performed pursuant to section 46(3) of the Act. See pp 60-61 of the report.

Reconciling the Definition of Substantial Performance with the Requirement for Certificate of Substantial Performance in Sections 2(1) and 43(1) of The Builders' Liens Act, C.C.S.M. c. B91

Canotech Consultants Ltd v. 599431 Manitoba Ltd., 2017 MBCA 48

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Manitoba
Author:
Joseph A. Pollock, Marr Finlayson Pollock LLP

CanLII References:

Court of Appeal

MANITOBA

28 Simply put, section 2(1) has a purpose other than the establishment of a date of substantial performance for the purpose of commencing the time period to register a lien pursuant to section 43(1).
(emphasis added)

The court determined that section 2(1) can be used to assist a payment certifier[5] or owner[6] in determining when a certificate of substantial performance should be issued, or a judge[7] where the payment certifier or owner fails or refuses to issue the certificate and a party is forced to apply to the court for an order that the contract has been substantially complete.

In the end, while the Court of Appeal reconciled the definition of substantial performance with the requirement for a certificate of substantial performance, the Court found that by virtue of the expectations of the parties that the plaintiff would continue to perform the contract until at least March of 2012, and the fact that the HVAC was not completed until the end of March, 2012, there was no need for the motions judge to consider the issue of the 40-day period in respect of completion of the contract. In arriving at this conclusion, the court relied upon that portion of section 43(1) of the Act which states that a claim for a lien by a contractor may be registered "during the performance of the contract". The Court found that since the plaintiff registered its lien during the performance of the contract, that alone made the lien valid.

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[5] **Certificate of substantial performance by payment certifier**

46(1) Where a contract requires a payment to be made upon a certificate of a payment certifier, the payment certifier, upon application by the contractor and upon being satisfied that the contract has been substantially performed, shall, within seven days after he receives the application or after the contract has, in his opinion, been substantially performed, whichever is the later, give or cause to be given a certificate of substantial performance of the contract in Form 8 of the Schedule to the contractor and the owner.

[6] **Certificate of substantial performance by owner**

46(2) Where a contract does not provide for payment to be made upon a certificate of a payment certifier, the contractor may, and on request of any of his sub-contractors shall apply to the owner for a certificate of substantial performance and the owner shall, within seven days after he receives the application or after the contract has, in his opinion, been substantially performed, whichever is the later, give or cause to be given a certificate of substantial performance of the contract in Form 8 in the Schedule to the contractor.

[7] **Judge's order for substantial performance**

46(3) Where a person required to give a certificate of substantial performance under subsection (1) or (2) fails or refuses to do so, the owner or the contractor or any subcontractor under the contractor or any person entitled to a lien in respect of the work under the contract may apply to a judge who, upon being satisfied that the contract has been substantially performed and that the certificate of substantial performance of the contract should have been given, may, upon such terms and conditions as to costs and otherwise as he deems just, make an order that the contract has been substantially performed, and the order has the same force and effect as if a certificate of substantial performance had been issued in respect thereof under subsection (1) or (2), as the case may be.

Canotech Consultants Ltd v. 599431 Manitoba Ltd., 2017 MBCA 48

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Manitoba
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CanLII References:

Court of Appeal

MANITOBA

Reconciling the Definition of Substantial Performance with the Requirement for Certificate of Substantial Performance in Sections 2(1) and 43(1) of The Builders' Liens Act, C.C.S.M. c. B91

Summary

1. Pursuant to subsection 43(1) of the Act, a claim for a lien by a contractor may be registered:

- before the performance of the contract;
- during the performance of the contract;
- within 40 days after substantial performance of the contract; or
- within 40 days after abandonment of the contract.

2. If a lien is not registered before or during the performance of a contract and the contract has not been abandoned, then the lien claimant must register a lien with within 40 days after substantial performance of the contract.

3. Substantial Performance occurs when a certificate of substantial performance has been issued by a payment certifier or an owner.

4. In determining when a contract has been substantially performed, a payment certifier or owner may look to section 2(1) of the Act for guidance.

5. When a payment certifier/owner fails or refuses to issue a certificate and a party is forced to apply to a judge for an order, the judge may look to section 2(1) of the Act for guidance in determining when a contract has been substantially performed.

Submission of Fixed, Instead of Unit Prices, Renders Bid Non-Compliant

Construction GCP inc. c. Ville de Saint-Jean-sur-Richelieu, 2017 QCCQ 12279 (CanLII)

LUC #146 [2018]

Primary Topic:
XII Tendering
Primary Topic:
III Building Contract
Jurisdiction:
Quebec
Author:
Etienne Paradis, Zaurrini Avocats

CanLII References:

QCCQ

QUEBEC

On February 25th, 2015, the City of Saint-Jean-sur-Richelieu (the "City") launched a public offering for the extensive construction works to be performed on the service building Poste Gouin (the "Project").

Since the costs associated with the Project exceeded $100,000, the City was required to proceed through a public offering in accordance with the procedure established by the *Cities and Towns Act* ("L.C.V.").

At the opening of the tenders, Construction G.C.P. Inc. ("G.C.P.") was the lowest bidder, however the City awarded the contract to the second lowest conforming bidder citing a major irregularity in G.C.P.'s tender.

According to the City, G.C.P. had not respected and therefore modified the terms of the tender documents by changing the price type for certain items, which disqualified it.

On the other hand, G.C.P. submitted that the inclusion of a fixed price rather than a unit price had no impact on the total price of the tender and therefore, did not affect the principle of equality among bidders. At most, it was a minor irregularity that did not allow for the rejection of its tender.

Consequently, G.C.P. was claiming the sum of $42,092.37 from the City for loss of profit as well as for the fees and costs it incurred to prepare its bid.

LAW

The Court had to determine whether the submission of a bid indicating pricing on a fixed price basis rather than a unit price required in the tender documents was a minor or major irregularity?

In order to assess the merits of G.C.P.'s claim, the Court recalled certain fundamental principles that govern the bidding process, namely the principle of equality among bidders.

The Court, citing Me Jasmin Lefebvre, reiterated that the principle of the equality among bidders is undoubtedly the most fundamental principle in matters of public offering because it ensures that all bidders must fulfill the same requirements in order for there to be a healthy competition between them.[1] Furthermore, the Court stated that the violation of this principle of

[1] *Are court requirements for bid compliance eroding? The point follows the decision in Structures GB inc. c. Ville de Rimouski, Revue du Barreau*, 168, printemps 2009, p. 254.

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Primary Topic:
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CanLII References:

QCCQ

QUEBEC

equality among bidders shall be the determining factor as to whether or not an irregularity is major or minor.

Thus, any non-conformity will not necessarily result in the rejection of a bid. A distinction must be made between a minor irregularity, which does not affect the objectives of a public offering and a major irregularity, which concerns an essential element or affects the fundamental objectives of the public offering.

The Court also revisited the Supreme Court decision *M.J.B. Entreprises*[2], which stated that the award of a contract to the lowest compliant bidder is the rule and that the client cannot derogate from this rule without legitimate reason or grounds to do so. That being said, the conformity of the bid to the tender documents was stated to be key.

Finally, the Court stated that the matter put before it must be examined in light of the tender documents for the Project and the other tenders received by the City, and therefore each case is a case in point.

DECISION

In the analysis of the case at bar, the Honorable Justice Monique Dupuis J.C.Q. analyzed the provisions and requirements of the tender documents for the Project and took into consideration clause 11.1 which provided that only the actual quantities will be paid to the Contractor. However, in the case of a fixed price contract, article 2109 of the *Civil Code of Québec* ("C.c.Q") would apply and thus prevent the City from claiming a price reduction:

> *« 2109. Where the price is fixed by the contract, the client shall pay the price agreed, and may not claim a reduction of the price on the ground that the work or service required less effort or cost less than had been foreseen.*
>
> *Similarly, the contractor or the provider of services may not claim an increase of the price for the opposite reason.*
>
> *Unless otherwise agreed by the parties, the price fixed by the contract remains unchanged notwithstanding any modification of the original terms and conditions of performance. »*
>
> [emphasis added]

[2] *M.J.B. Enterprises Ltd.* c. *Construction de Défense (1951) Ltée*, [1999] 1 R.C.S. 619 .

Construction GCP inc. c. Ville de Saint-Jean-sur-Richelieu, 2017 QCCQ 12279 (CanLII)

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CanLII References:

QCCQ

QUEBEC

Submission of Fixed, Instead of Unit Prices, Renders Bid Non-Compliant

As such, the Court concluded that the fixed price submitted by G.C.P. would preclude the application of Clause 11.1 during the execution of the Contract since the City would now be required to pay the fixed price submitted by G.C.P., even if the actual quantities were less than those provided in the tender documents.

Furthermore, G.C.P. voluntarily modified the tender documents by entering a fixed price rather than a unit price as stipulated and, as a result, it modified the conditions of the tender documents for the Project. In addition, the Court recalled that a contractor cannot negotiate with the client at the stage of "Contract A", formed by the public offering process, since this would be contrary to the principle of equality between bidders.

CONCLUSION

For these reasons, the Court found that G.C.P.'s bid was not in conformity with the tender documents because it submitted a fixed price for certain items of the tender documents which required a unit pricing and this constituted a major irregularity. The Court found that the City was justified in excluding G.C.P.'s bid, and therefore dismissed G.C.P.'s claim with costs.

This recent decision by the Court of Quebec demonstrates how important it is for contractors to pay particular attention to the requirements of the tender documents, especially those regarding pricing methods, since this may result in the disqualification of their tender.

Construction GCP inc. c. *Ville de Saint-Jean-sur-Richelieu*, 2017 QCCQ 12279 (CanLII)

Le 25 février 2015, la ville de Saint-Jean-sur-Richelieu (« la Ville ») lance un appel d'offres pour l'exécution de travaux d'agrandissement du bâtiment de service au Poste Gouin (« le Projet »).

Considérant qu'il s'agit d'un projet de plus de 100 000$, la Ville doit procéder par appel d'offres public suivant la procédure établit par la *Loi sur les cités et villes* (« L.C.V. »).

À l'ouverture des soumissions, l'entrepreneur Construction G.C.P. Inc. (« G.C.P.») est le plus bas soumissionnaire, mais la Ville accorde cependant

Submission of Fixed, Instead of Unit Prices, Renders Bid Non-Compliant

Construction GCP inc. c. Ville de Saint-Jean-sur-Richelieu, 2017 QCCQ 12279 (CanLII)

LUC #146 [2018]

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XII Tendering
Primary Topic:
III Building Contract
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Quebec
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CanLII References:

QCCQ

QUEBEC

le contrat au deuxième plus bas soumissionnaire invoquant une irrégularité majeure dans la soumission de G.C.P.

En effet, selon la Ville, G.C.P. a changé les conditions de l'appel d'offres en modifiant le type de prix à l'égard de certains éléments, ce qui disqualifie sa soumission.

De son côté, G.C.P. plaide que le fait d'inscrire un prix forfaitaire plutôt qu'un prix unitaire n'a aucune incidence sur le prix total de la soumission et sur le principe de l'égalité entre les soumissionnaires. Il s'agit tout au plus d'une irrégularité mineure ne permettant pas le rejet de sa soumission.

Conséquemment, G.C.P réclame à la Ville la somme de 42 092,37 $ pour la perte du profit qu'elle aurait fait si elle avait obtenu le contrat.

LE DROIT

Dans le dossier sous étude, considérant que G.C.P. avait soumis un prix forfaitaire à l'égard de certains éléments du bordereau de soumission au lieu d'un prix unitaire, tel que demandé dans les documents d'appel d'offres, le Tribunal devait décider si ladite soumission était entachée d'une irrégularité majeure ou mineure, et donc, si la Ville était justifiée de la rejeter.

Afin d'évaluer le bien-fondé de la demande de G.C.P., le Tribunal rappelle certains principes en matière d'appel d'offres, plus particulièrement le principe de l'égalité des soumissionnaires.

Le Tribunal, citant Me Jasmin Lefebvre, rappelle que le principe de l'égalité des soumissionnaires est sans aucun doute le principe le plus fondamental en matière d'appel d'offres et que tous les soumissionnaires doivent respecter les mêmes exigences, afin qu'il y ait une saine compétition entre eux[1].

Au surplus, le Tribunal est d'avis que le principe de l'égalité des soumissionnaires constitue le facteur déterminant pour qualifier une irrégularité de majeure ou mineure.

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[1] *Les exigences des tribunaux quant à la conformité des soumissions sont-elles en processus d'érosion? Le point suite à la décision dans Structures GB inc. c. Ville de Rimouski*, Revue du Barreau, t. 168, printemps 2009, p. 254.

Submission of Fixed, Instead of Unit Prices, Renders Bid Non-Compliant

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LUC #146 [2018]

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Primary Topic:
III Building Contract
Jurisdiction:
Quebec
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CanLII References:

QCCQ

QUEBEC

Ainsi, toute non-conformité n'est pas nécessairement de nature à entraîner le rejet d'une soumission. Il faut distinguer entre « une irrégularité mineure qui ne porte pas atteinte aux objectifs des appels d'offres et une irrégularité majeure, qui porte sur un élément essentiel ou qui touche les objectifs fondamentaux du processus d'adjudication par voie de soumission ».[2]

Reprenant la Cour suprême dans l'affaire *M.J.B. Entreprises*[3], le Tribunal précise également que la conclusion d'un contrat avec le plus bas soumissionnaire conforme est la règle et que le donneur d'ouvrage ne peut y déroger sans motif légitime.

Cela dit, la conformité de la soumission est un point central dans l'analyse des soumissions déposées et la Ville doit seulement accorder le contrat au plus bas soumissionnaire qui est conforme.
Le Tribunal précise finalement qu'il faut analyser cette question en fonction des documents d'appel d'offres et des soumissions déposées, et que chaque cas est un cas d'espèce.

L'ANALYSE

Dans le cas sous étude, le Tribunal analyse les dispositions et exigences de l'appel d'offres et prend en considération la clause 11.1 à l'effet que « seules les quantités réelles seront payées à l'Entrepreneur ». Or, dans le cas du contrat à forfait, l'article 2109 du *Code civil du Québec* (« C.c.Q. ») s'appliquerait et empêcherait la Ville de prétendre à une diminution de prix :

> « 2109. Lorsque le contrat est à forfait, le client doit payer le prix convenu et il ne peut prétendre à une diminution du prix en faisant valoir que l'ouvrage ou le service a exigé moins de travail ou a coûté moins cher qu'il n'avait été prévu.
>
> Pareillement, l'entrepreneur ou le prestataire de services ne peut prétendre à une augmentation du prix pour un motif contraire.
>
> Le prix forfaitaire reste le même, bien que des modifications aient été apportées aux conditions d'exécution initialement prévues, à moins que les parties n'en aient convenu autrement. »
>
> [Nos soulignements]

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[2] Paragraphe [40].
[3] *M.J.B. Enterprises Ltd.* c. *Construction de Défense (1951) Ltée*, [1999] 1 R.C.S. 619

Construction GCP inc. c. Ville de Saint-Jean-sur-Richelieu, 2017 QCCQ 12279 (CanLII)

LUC #146 [2018]

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CanLII References:

QCCQ

QUEBEC

Submission of Fixed, Instead of Unit Prices, Renders Bid Non-Compliant

Ainsi, le Tribunal est d'avis que le prix forfaitaire soumis par G.C.P. empêcherait l'application de la clause 11.1 au cours de l'exécution du contrat puisque la Ville serait tenue de payer le prix forfaitaire soumis par G.C.P., et ce même si les quantités réelles étaient moindres que celles prévues dans l'appel d'offres.

En outre, G.C.P. a modifié volontairement le bordereau de soumission en inscrivant un prix forfaitaire plutôt qu'un prix unitaire, modifiant ainsi les conditions de l'appel d'offres. Or, le Tribunal rappelle qu'un entrepreneur ne peut négocier avec le donneur d'ouvrage au stade du Contrat A, formé par l'appel d'offres, puisque cela serait contraire au principe de l'égalité entre les soumissionnaires.

CONCLUSION

Pour ces motifs, le Tribunal conclut donc que le fait pour G.C.P. d'avoir soumis un prix forfaitaire à l'égard de certains éléments du bordereau de soumission au lieu d'un prix unitaire, tel que demandé dans les documents d'appel d'offres, constitue une irrégularité majeure. Le Tribunal décide que la Ville était justifiée d'écarter la soumission de G.C.P., et rejette ainsi l'action de l'entrepreneur.

Cette décision de la Cour du Québec démontre bien à quel point il est important pour les entrepreneurs de porter une attention particulière aux exigences des appels d'offres, plus particulièrement sur les modalités de fixation des prix, puisque cela peut parfois entrainer la disqualification de leur soumission.

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Ontario
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ONTARIO

Bill 142

Bill 142, the Bill introduced to amend Ontario's *Construction Lien Act* received Royal Assent on December 12, 2017. While the Bill passed with relative speed through the Ontario Legislature, its full transition into law will be more gradual.

As stated in section 85 of the *Construction Lien Amendment Act, 2017*, the housekeeping and non-substantive amendments came into force on the date the Bill received Royal Assent. The substantive amendments will come into force on a date proclaimed by the Lieutenant Governor. The amendments affecting the lien and holdback process will come into force first, with the prompt payment and adjudication provisions to follow suit once an adjudicative body has been established. The Government of Ontario has stated that they will provide notice to stakeholders prior to any amendments coming into force. Draft regulations to the *Construction Lien Amendment Act, 2017* are expected to be released soon.

The *Construction Lien Act*, as it is read immediately before the day subsection 2(2) of the *Construction Lien Amendment Act, 2017* came into force, continues to apply to an improvement if:

1) a contract for the improvement was entered into before that day, regardless of when any subcontract under the contract was entered into;

2) a procurement process, if any, for the improvement was commenced before that day by the owner of the premises; or

3) the premises is subject to a leasehold interest, and the lease was first entered into before that day.

The date that s. 2(2) comes into force has not yet been determined. However, the current Act will continue to apply to existing contracts, even those that are presently still in the procurement stage. It is important to note that the current statute will not disappear overnight. It is not unusual for big construction projects to take years. There will be long term leases still subject to the present Act. The present statute will be transitioned out gradually, counsel will need to be alert to whether the new or old Act applies during this gradual transition.

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
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Ontario
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ONTARIO

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

Parts I.1, Prompt Payment, and II.1, Construction Dispute Interim Adjudication, apply in respect to contracts and subcontracts entered into on or after the day subsection 11(1) of the *Construction Lien Amendment Act, 2017* comes into force. The date that s. 11(1) comes into force is not set, but is anticipated to be later than s. 2(2). The industry will have some time to get ready for prompt payment and adjudication, and it is apparent that the current regime will continue to apply for existing work and procurement processes.

The enactment of Bill 142 will bring four major changes to the construction industry. We highlight four of the most critical: the extended timeframe to preserve and perfect liens; mandatory release of holdback; prompt payment; and mandatory adjudication.

Deadline to Preserve and Perfect Liens

Prior to the enactment of Bill 142, the timeframe to preserve a lien was 45 days, and to perfect a lien was 45 days from the last day it could be preserved. These deadlines have been extended pursuant to sections 31 and 36 of the *Construction Lien Amendment Act, 2017*, to 60 days and 90 days respectively. Under the new legislation, the total lien perfection period to start a court action is 150 days, an increase from 90 days under the *Construction Lien Act*. Bear in mind our comments on transition, this will not apply to existing contracts and subcontracts, only to new contracts entered into after s.2(2) comes into force.

Holdback

The wording of sections 26 and 27 of the *Construction Lien Act*, pertaining to the release of holdback once the lien period has expired and no liens are left on title, have changed from a permissive "may" to a mandatory "shall". It will now be mandatory for holdback to be released. It is possible for the Owner to claim a set-off, but this must be done via a "Notice of Non-Payment due to Set-Off", listing claims and amounts of claimed set-off.

Phased, annual or segmented release of holdback will be allowed under the *Construction Lien Amendment Act, 2017*. However, release of holdback in these situations will be restricted. Phased or annual release of holdback will be limited to large, multi-year projects. Segmented holdback will be allowed on projects with clearly separable improvements. Deferral Agreements may also be entered into, which will allow for the exclusion of portions of work

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Ontario
Authors:
Brendan D. Bowles and Emma Cosgrave (Student at Law), Glaholt LLP

ONTARIO

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

from the calculation of substantial performance so as to allow for early holdback release. Again, these new holdback rules apply only to new contracts entered into after s. 2(2) comes into force.

Prompt Payment

Bill 142 provides for a prompt payment regime, applying to all public and private sector construction contracts. The *Construction Lien Amendment Act, 2017*, requires payment within 28 days from the Owner to the General Contract upon the submission of a "Proper Invoice" by the General Contractor. The regime also requires payment to be made from the General Contractor to the sub-contractor within 7 days of the General Contractor's receipt of payment from the Owner. However, the Owner, General Contractor or other payer will be allowed to set off against "Proper Invoices" submitted by submitting a "Notice of Intention to Withhold Payment" within 7 days of receipt of a "Proper Invoice". We are some time away from actual implementation, the prompt payment provisions will apply to contracts entered into after s. 11(1) comes into force. This will be later than the aforementioned s.2(2) reforms, so expect the rollout of prompt payment in Ontario to be gradual.

There were concerns with the prompt payment provisions as Bill 142 was going through its first, second and third reading. These concerns mainly pertained to the payment enforcement mechanisms within the Bill. It appears that these concerns have been heard and addressed. With the new legislation, it is possible to initiate an adjudication proceeding, for the contractor or subcontractor to legally suspend work until paid, reimbursement of reasonable costs incurred, and there is mandatory payment of interest. If the matter proceeds to adjudication, the Determination, with reasons, is filed with the Court and is subject to the same enforcement as any Court Order. This means that parties who disregard the adjudicator's Determination will, *inter alia*, be subject to garnishment, seizure of property, and invasive examinations in aid of execution.

Mandatory Adjudication

The mandatory adjudication provisions are to be read into all Ontario construction contracts. The Bill allows parties to the contracts to create contractual adjudication regimes, subject to the regime being consistent with the *Construction Lien Amendment Act, 2017*. Any party to the contract or subcontract will have the ability to refer disputes to adjudication. Lien rights are maintained while the dispute progresses through adjudication.

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

LUC #146 [2018]

Primary Topic:
IX Construction and Builders' Liens
Jurisdiction:
Ontario
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ONTARIO

Legislative Update – The Progress of Bill 142 in the Ontario Legislature

The adjudication process within the Bill has been streamlined to efficiently limit the amount of time the issue remains in dispute. In order for the adjudication process to commence, a party must submit a Notice of Adjudication. There will then be 4 days for the parties to agree upon and choose an adjudicator, or 7 days for the nominating body to decide. The parties are then given 5 days to prepare a "Referral Notice", including the Notice of Adjudication and any relevant documents to the dispute to the Adjudicator. The Adjudicator will then have 30 Calendar Days to investigate, gather evidence, retain experts as needed, interview individuals involved and render a decision. The decision will be binding on an interim basis.

Prior to Royal Assent of the Bill, MPP's expressed concern that the written decisions of adjudicators would only be made available to the parties involved in the dispute, thus not providing precedents for future adjudications. The reasoning of the Adjudicator will be filed with the Determination; the Government of Ontario has permitted publicity by allowing parties to file the Determination with the Court. However, it is not clear to us whether the decisions will be easily accessible or searchable, for example on CanLii or Westlaw.

Concerns of whether parties will have sufficient protection from bad adjudicative decisions was also raised in the House prior to the Bill receiving Royal Assent. The aim of Bill 142 is to reduce the frequency with which construction disputes end up in court. Creating an appeal mechanism creates an unwarranted secondary litigation process that would frustrate the purpose of implementing an adjudication scheme, namely, the loss of prompt, binding decision making on an interim basis during the project. Moreover, a party who is unhappy with an adjudicator's decision can always enter into litigation after the project is over. There will also be an ability to bring an Application for Judicial Review of an adjudicator's decision where warranted. The Legislature appears to have found a balance in allowing for challenge of biased or flawed adjudication processes, while preserving the summary. It bears repeating that the transition to adjudication will be gradual, and will only apply to contracts entered into after s. 11(1) comes into force.

Conclusion

The *Construction Lien Amendment Act, 2017*, is obviously a significant development in Ontario, but warrants national attention insofar as reforms to the holdback rules, prompt payment and adjudication present hope for more expeditious and proportionate resolution of most construction disputes. Once the substantive amendments to the Act are in force and begin to apply to new construction contracts, the implementation of these reforms will no doubt merit close attention across Canada. We now look forward to the draft regulations, which are the next steps in this legislative process and which will be crucial to the interpretation and application of the Act.

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LegalUpdate117	2013	117	Full text of newsletter	I. General
LegalUpdate116	2013	116	Full text of newsletter	I. General
LegalUpdate115	2013	115	Full text of newsletter	I. General
LegalUpdate114	2013	114	Full text of newsletter	I. General
LegalUpdate113	2013	113	Full text of newsletter	I. General
LegalUpdate112	2013	112	Full text of newsletter	I. General
LegalUpdate111	2012	111	Full text of newsletter	I. General
LegalUpdate110	2012	110	Full text of newsletter	I. General
LegalUpdate109	2012	109	Full text of newsletter	I. General
LegalUpdate108	2012	108	Full text of newsletter	I. General
LegalUpdate107	2012	107	Full text of newsletter	I. General
LegalUpdate106	2012	106	Full text of newsletter	I. General
LegalUpdate105	2012	105	Full text of newsletter	I. General
LegalUpdate104	2012	104	Full text of newsletter	I. General