

A Layperson's Guide to the *Construction Act*



Hamilton • Halton Construction Association

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OVERVIEW TO ‘THE LAYPERSON’S GUIDE TO THE *CONSTRUCTION ACT*’

The Government of Ontario has long recognized that the construction industry is a volatile industry requiring some measure of protection for those companies and individuals supplying labour and materials to job sites. In 1983, the Government enacted the *Construction Lien Act* to replace the **Mechanic’s Lien Act**.

The new *Construction Act* (“Act”) has not yet come in to force and the regulations have not been finalized. The effective dates will be:

- July 1, 2018 – Amendments to liens and holdback rules
- October 1, 2019 – Amendments dealing with prompt payment, adjudication and municipalities

The Act represents a complete overhaul of the existing *Construction Lien Act* (the “Former Act”) which was enacted in 1983, with only minimal amendments having been made since then.

Prompt payment and adjudication are brand new substantive regimes introduced for the first time in the Act. The *Construction Act* is a creature of the legislature and creates a procedural scheme designed to have disputes resolved in a more summary fashion than is ordinarily available. It allows for those having a direct contract with one another to have their rights and responsibilities defined but also provides rights and responsibilities for those in the construction pyramid, even where a direct contract is not found.

The rights and obligations can be separated into several categories:

- 1) lien rights
- 2) holdbacks;
- 3) trust obligations;
- 4) prompt payment; and
- 5) adjudication

Please understand that the Act’s extensive changes from prior legislation have not been tested in courts and therefore judicial interpretation of the new sections has not yet taken place and could alter the impact of certain parts of the new Act.

This guide is not to be taken as legal advice. The authors, although lawyers, are not providing you with legal advice in this guide. The authors and the Ottawa Construction Association will not accept any liability for your reliance on the information in this guide. It is meant as an introduction to the new *Construction Act*. If you require legal advice, contact an Ontario lawyer for such advice.

LIEN RIGHTS

What is a construction lien?

A construction lien is a registration on title to a property. Think of it as a mortgage. When you obtain a mortgage, the bank will loan you money and will register a mortgage on title to your home. A mortgage gives the bank the ability to sell your house and get paid before anyone else in the event you fail to pay your mortgage.

A construction lien gives the lien claimant that same ability. If you are owed money on a construction project, you can register a lien to seek payment. It also gives you the ability to sell the property and to seek to get paid before anyone else.

Why would you lien?

A lien can give you “security”, in that there is an asset that belongs to you if you can prove a lien. Security can see you paid even in the event of a bankruptcy.

A lien can also entitle you to be paid out of holdback funds that are required to be retained.

Who can lien?

Any person who is under a contract and has supplied services and/or materials to an “improvement” has a right to lien. Pretty well all persons working on a construction project will have a right to lien, including suppliers of rental equipment, architects, and those who provide design services.

What can you lien?

The Act makes reference to an “*improvement*” to set out what type of property and what type of work can be liened.

An improvement includes the alteration of and/or the addition to the property. This is a broad definition and encapsulates most construction activity.

It also includes the construction and installation of industrial, mechanical, or electrical equipment, when that equipment is essential to the regular use of that property. Affixed machinery in a plant such as an automotive assembly plant would fall within the definition of an improvement.

It is also possible to lien for work done for a capital repair. This type of work is for work done to extend the economic life of a building or structure. It has to be noted that this does not include just any type of repair, and does not include preventative maintenance.

Can you lien when doing work for a tenant?

The short answer is yes. However, whether your lien will affect the rights of the landlord or the tenant will depend. If your work is solely within the tenant's space, then you cannot tie the landlord to your work. If, however, your work is connected to both the tenant's space and the landlord's building or land, you may have a right to claim from the landlord.

If your work is only related to the tenant's interest, you may still be able to recover from the landlord. In the event that the lease calls for payment by the landlord to the tenant, the landlord may be liable to the lien claimant for 10% of the value of the payment.

Can you lien a public road or a street?

Yes, although a lien does not "attach" to title in the same way. Rather than register a lien on title you preserve it by providing certain people with the lien.

Can you lien government or municipal property?

Federal Government Property - Federal government property cannot have liens enforced against them. The Federal Government takes the position that the Act has no application at all to its property.

Generally, most Federal projects are protected by Labour and Material Payment Bonds, which can be utilized by trades and suppliers to obtain payment.

Provincial Government Property - Provincial government property is subject to the Act. The lien is preserved by providing the government body in charge of the project with the lien.

The property is never "sold" to enforce the lien, rather the lien acts as a mechanism to be entitled to share in the holdback.

If the contract is in excess of a prescribed amount (yet to be prescribed as of the date of this guide), then a labour and material payment bond, in an amount of at least 50% of the contract value, is required. Similarly, a performance bond is also required in an amount of at least 50% of the contract value.

Municipal Government Property - Municipal property is subject to the Act. The lien is preserved by providing the clerk of the municipality with a copy of the lien.

Similarly, the property is never "sold" to enforce the lien, rather the lien acts as a mechanism to be entitled to share in the holdback. If the contract is in excess of a prescribed amount (yet to be prescribed as of the date of this guide), then a labour and material payment bond, in an amount of

at least 50% of the contract value, is required. Similarly, a performance bond is also required in an amount of at least 50% of the contract value.

What work can you lien for?

Supply of services can include engineering and architectural services or the rental of equipment and has been extended to include the supply of security services to a construction site or the services of estimating and job supervision

What is the value of your lien?

The Act gives you the ability to lien for the “price” of services and materials that you provided to the project. “Price” is a defined term and means:

- the amount agreed between the parties, or if there is no agreement on the amount, then the market value of the work; AND
- any direct costs incurred as a result of a delay.

Direct costs are lienable if they are costs that arise directly from a delay. These will include items such as additional bond premiums, equipment rentals, additional labour, and costs related to seasonal conditions.

You are **not** entitled to lien for interest on the amount you are owed, nor can you lien for any indirect costs associated with your claim. For instance, on project that has been delayed, you cannot lien for extended overhead or head office costs, loss of productivity, or loss of profit.

It must be pointed out that while you cannot lien for these amounts, you are still at liberty to assert a claim for the amounts as part of a claim under regular contract law.

It must also be pointed out that you should never exaggerate the value of your lien. The Act contains specific provisions about an “exaggerated” lien and that you could be liable for the costs that someone incurs as a result of the exaggerated lien.

When can you lien?

Once you have supplied materials or services to site, you have a lien. You can register a lien even though the money is not yet due and owing and if you have yet to render an invoice. In theory, you could register a lien every day you are on site even though you have not invoiced for the work. In practice, that is a terrible idea.

By when do you have to preserve lien?

The authors cannot emphasize enough the strict timelines that are outlined in the Act. If you

miss a deadline, you will lose your right to lien and may not see any payment.

Before you start to count days, you first have to determine whether you are a “*contractor*” or a “*subcontractor*”. A “contractor” has a contract directly with the owner. A “subcontractor” is anyone with a contract with the contractor, or with another subcontractor (i.e. a supplier).

Lien of a Contractor

A contractor must register its lien within 60 days of the earlier of:

- the date upon which the certificate of substantial performance is published (if there is one); and
- the date that the contract was completed, abandoned, or terminated.

Lien of a Subcontractor

A subcontractor, or any other person, must register its lien within 60 days of the earlier of:

- the date upon which the certificate of substantial performance is published (if there is one);
- the date that they last supply services or materials to the project;
- the date that the contract was completed, abandoned, or terminated; and
- the date that the subcontract is certified to be complete (this rarely occurs).

Certificate of Substantial Performance

Not all construction projects will carry with them a requirement for a certificate of substantial performance (“**CSP**”).

A CSP can be published by a payment certifier (i.e. architect) if there is one, or by the owner and contractor. The CSP serves as notice that the project is almost complete, and acts to cut off a significant portion of lien rights.

A CSP can only validly be published when two criteria are met:

1. When the project, or a majority of the project, is ready for the use for which it is intended (i.e. a residential property is ready to be occupied); and
2. Where the project is can be completed for (or the value of a known defect is) not more than:

- a. 3% of the first \$1,000,000 of the contract price;
- b. 2% of the next \$1,000,000 of the contract price; and
- c. 1% of the balance of the contract price.

For example, on a \$1,000,000 project, the defect/correction has to be worth less than \$30,000. On a \$4,000,000 project, the defect/correction has to be worth less than \$70,000

In the event that your work is done both before and after the CSP, you will in effect have 2 liens. You will have to lien within 60 days for all work done up to the date of the CSP, and then lien within 60 days of either your last day of supply or when your contract comes to an end (depending on whether you are a contractor or subcontractor).

In order to search for a CSP, you can go online to the following website and input details relating to the project

<https://canada.constructconnect.com/dcn/certificates-and-notice>

When is a contract or subcontract complete?

The completion of a contract will depend on the facts of each case. However, a contract is “deemed” to be complete when the price of completion, the correction of a known defect, or the last supply is of a value of less than the lower of:

1. 1% of the contract price; and
2. \$5,000

For example, if the value of your contract is \$1,000,000, it will be “deemed” to be complete if you have less than \$10,000 worth of work left.

Can you extend your lien rights? What is your last day on site?

People often enquire if they can attend back on site and hammer a nail in to extend lien rights. Unless you are returning to the project to complete some significant contract work, your lien rights will expire. You cannot return to the site and supply a drywall screw in the hopes of reviving your lien rights. Furthermore, you cannot claim your last day of supply was when you returned to complete deficiency work.

Do days include weekends and holidays?

Yes, when counting the relevant days, you must count weekends and holidays. However, if your 60th day lands on a weekend or holiday, then you are permitted to preserve your lien on the following business day.

Notice of Termination

In the event that a contract or a subcontract is terminated, a notice is required to be published. As at the time of writing this, the details of how the notice is published is not available.

Written Notice of a lien

The first step which you may wish to consider prior to the actual registration of a lien is a written notice of lien. Typically this can be used in the event that your lien rights do not expire for a period of time that will permit the written notice to have time to be effective.

A written notice of a lien is completed by personally serving a prescribed form on the person(s) above you in the construction pyramid (as of the date of this guide, there is no form). Upon receipt of a written notice of lien, the payer, i.e. the person above you in the construction pyramid, must retain the full amount in dispute.

The written notice of a lien is only a temporary measure. It does not stop your clock from running on the time you have to register your lien. Furthermore, if you are still unpaid after the written notice of lien is sent, you still need to register your lien on title or you will lose your lien rights.

How do you register a lien?

The act of placing a lien on title is known as “*preserving*” your lien. It is the registration of your lien on title.

There is a specific form that has to be completed, with information such as:

- your proper legal name;
- who you contracted with;
- the name of the owner;
- the time in which you supplied to the project;
- your total contract value;
- how much you are owed;
- what type of work you supplied;

This can be done by visiting the local Land Registry Office in the county of the project. In Ottawa, the Land Registry Office is located at the courthouse at 161 Elgin Street. Lawyers have access to a program called Teraview which allows them to register your lien electronically.

What happens after you register your lien?

Once the lien is registered, you will have to “*perfect*” the lien by starting a court action. This cannot be done in Small Claims Court even if the value of the lien is less than the \$25,000 limit. The claim is issued in the Superior Court, and it has to be done within 90 days of the last day in which you could have registered your lien.

After the statement of claim is issued, a certificate of action also has to be issued, and then registered on title of the property.

If you fail to commence the court action, or fail to register the certificate of action, your lien will expire and it cannot be enforced.

Once the court action is commenced, it proceeds through the litigation process similar to any other lawsuit. There are some modifications to the process that do differ from an ordinary lawsuit. There is no automatic disclosure of documents, no right to examinations for discovery, and no mandatory mediation. However, it is usually agreed between the parties that these steps will take place, depending on the nature of the matter.

In order to maintain your lien, you will have to take steps to advance the court action. Within two years of starting the claim, you will have to ensure that it is set down for trial or that there has been an Order directing a trial. If this is not done, your lien will expire.

Can I agree that the Act does not apply to me?

No, you cannot “contract out” of the Act. The provisions apply to you no matter what, so you cannot have provisions in a contract that prevent a person from liening, or that holdbacks are not required.

What if you make a mistake with the lien?

There are limited ways in which a CSP or a claim for lien can be fixed. If the mistake is minor, such as if the name of the owner is incorrect or the legal description of the land is incorrect, then a court can decide that the lien or certificate (as the case may be) is still valid.

However, great care still has to be taken to ensure that no mistake is made.

How do you get a lien off title?

If you are unable to come to a resolution, it may be necessary to have the lien removed from title.

You can bring a motion to court, without telling the lien claimant, so long as you pay into court cash, a lien bond, or a letter of credit in the amount of the lien plus 25%. You will obtain a court order that you register on title of the property that removes the lien, and the court action

proceeds. The court action proceeds with money in court being recoverable by the lien claimant at the end of the day.

If a lien is out of time or is otherwise invalid, you can bring a motion to declare that the lien is invalid. If you are successful, the lien is deleted. However, this does not prevent a breach of contract claim from continuing.

Priority Of Liens

Rules surrounding priorities are complex.

There are circumstances where a lien can take priority over a mortgage, but it is often limited. It will depend on when your lien arose, when the mortgage was registered, the type of mortgage, and the date of mortgage advances.

HOLDBACKS

The Basic Holdback

For the specific protection of those not having a direct contract with others above them in the construction pyramid, the Act provides a requirement that a basic holdback of 10% be maintained by each “*payer*”. In other words, each owner, contractor, and subcontractor has to withhold 10% of each payment that they make. The 10% is the notional profit that the payer or trade would be earning on the project, so the Act contemplates receiving a profit at the end of the project.

The balance of 90% can be paid by a payer, unless the payer has received a written notice of lien or a claim for lien.

The Notice Holdback

In the event of receipt of a written notice of lien or receipt of a claim for lien, the payer must maintain a notice holdback, which must be equal to the amount in dispute. If they do not, then the payer may effectively have to pay twice for the work.

For example, if a subcontractor on a project registers a lien and provides that lien to the owner of the project, the owner has to withhold from the general contractor the amount of that lien.

Entitlement to Holdback

The basic holdback and notice holdback combined will be available to those who prove valid lien. You must have a lien to be entitled to holdback. In the event that there is sufficient holdback to see the lien claims paid, they may be paid in full. In the event that the holdback is less than the value of all of the liens, the lien claimants will share pro-rata in the holdback.

Release of Holdback

The prior provision for the release of holdback was not mandatory. The new provision is mandatory and provides for a mandatory release after all liens that may be claimed against the holdback have expired. By using tracked changes, we can show you the old and new legislation in the following excerpt:

Payment of basic holdback

26. ~~Each~~ Subject to section 27.1, each payer upon the contract or a subcontract ~~may, without jeopardy, shall~~ make payment of the holdback the payer is required to retain by subsection 22 (1) (basic holdback), so as to discharge all claims in respect of that holdback, where all liens that may be claimed against that holdback have expired ~~as provided in Part V, or have~~ been satisfied, discharged or otherwise provided for under ~~section 44~~ this Act. R.S.O. 1990, c. C.30, s. 26.

An owner can refuse to pay the holdback, or a portion of it, only if they give notice to the contractor and they publish a notice (which is yet to be prescribed as of the date of this guide). In the event this happens, a contractor can then refuse to pay holdback only if they refer the matter to adjudication and they notify all subcontractors. The process repeats for other payers in the construction pyramid.

Parties may agree to the annual release of holdback if the following conditions have been met:

1. the contract provides for a completion schedule longer than one year;
2. the contract provides for the annual payment of holdback;
3. the contract price is higher than the prescribed amount (not yet prescribed as of the date of this guide); and
4. there are no registered liens at the time of the payment date.

Parties may agree to the phased release of holdback if the following conditions have been met:

1. the contract provides for the phased release of holdback and identifies the phases;
2. the contract price is higher than the prescribed amount (not yet prescribed as of the date of this guide);
3. there are no registered liens at the time of the payment date.

Finishing Holdback

The Act provides for finishing holdbacks, being 10% of the value of the work completed. Finishing holdbacks are for the work completed after the publication of a CSP. You may register a lien against the finishing holdback, but that work must have been completed after the publication of the CSP.

RIGHTS TO INFORMATION

Any person working on a project has the right to receive certain information from others. You do not need to have registered a lien to be entitled to the information. The request can be made by that person, and the recipient is required to respond within 21 days.

Why do you want this Information?

This is important to determine whether those above you in the construction pyramid have received payments themselves. It can also provide valuable information concerning a Labour and Material Payment Bond that might be available to satisfy claims of those who may have missed out on their limitation period for filing a claim for lien. It can also help you determine if you can try to claim a priority over a mortgage or whether there may be liability on a landlord.

Information from the Owner or a Contractor

You are entitled to the following information:

- the names of the parties to the contract,
- the contract price,
- a state of accounts between the owner and the contractor containing certain information (explained below),
- a copy of any labour and material payment bond,
- a statement of whether the contract provides that liens arise and expire on a lot-by-lot basis, and
- a statement of whether the contract provides that payment is based on the completion of specified phases or the reaching of other milestones in its completion.

If an owner is selling a “home” (i.e. a residential property or condominium unit), you are entitled to the following information:

- the name and address of the purchaser, the sale price, the amount of the purchase price paid or to be paid prior to the conveyance, the scheduled date of the conveyance and the lot and plan number or other legal description of the premises, and
- the date that the occupancy permit was issued.

Information from a Contractor or Subcontractor

You are entitled to the following information:

- the names of the parties to the contract,
- a state of accounts between the contractor and a subcontractor, or between a subcontractor and subcontractor, containing certain information (explained below),
- a statement of whether there is a provision in a subcontract providing for certification of the subcontract,
- a statement of whether a subcontract has been certified as complete, and
- a copy of any labour and material payment bond,

Information from a Landlord

You are entitled to the following information:

- the names of the parties to the lease,
- the amount of the payment that the landlord has paid to the tenant for the work, and
- a state of accounts between the owner and the contractor containing certain information (explained below),

Information from a Mortgagee

You are entitled to the following information from someone that holds a mortgage on the property:

- sufficient details to allow you to determine if the mortgage was used for the building of the project;
- a statement showing the amounts advanced under the mortgage; or
- a statement showing the amount secured under the agreement of purchase and sale and any arrears in payment including any arrears in the payment of interest

What information is required in the statement of accounts?

An owner, contractor, or subcontract is required to advise you:

1. The price of the services or materials that have been supplied under the contract or subcontract.
2. The amounts paid under the contract or subcontract.
3. In the case of a landlord, which amounts are paid on account of an improvement.
4. The amount of the applicable holdbacks.
5. The balance owed under the contract or subcontract.
6. Any amount retained as a set off.
7. Any other information that may be prescribed (none as of the date of the guide)

TRUST OBLIGATIONS

The trust provisions are separate and apart from the lien provisions. You do not need to have a lien in order to claim a trust.

What is a trust?

A “trust” is the holding of property that belongs to someone else.

What is the trust under the *Construction Act*?

All persons in the construction pyramid, when they received money from those above them in the pyramid, are holding those funds in trust for those below them in the pyramid. For instance, when the general contractor receives a progress payment, that money is held in trust for the subcontractors that performed work. Until all of those subcontractors have been paid in full the contractor must not appropriate or convert any part of the trust funds for its own use or any use not authorized by the Act.

There are six different types of trusts that can be created by the *Construction Act*. They are:

1. Mortgage Trust
2. Substantial Performance Trust
3. Purchaser’s Trust
4. Certificate Trust
5. Draws Trust
6. Vendor’s Trust

Mortgage Trust

All moneys received by an owner to be used in the financing of an improvement (usually under the form of a building mortgage) constitute a trust fund for the benefit of the contractor.

Certificate Trust

On some construction projects, the owner will engage the services of an architect or an engineer to prepare plans and specifications and to supervise the construction. In order to facilitate the flow of payments down the construction pyramid from the owner to contractor to subcontractors to sub-subcontractors, the architect/engineer may issue certificates from time to time certifying

what work was completed and placing a dollar value on that work. The amount certified by this certificate constitutes a trust fund for the benefit of the contractor providing that the money is actually in the owner's hands or received by the owner after the certification.

Substantial Performance Trust

This trust is only created where substantial performance of the contract has been certified under the Act. Where the owner has only made part payment of the certified amount to the contractor, the unpaid portion constitutes a trust providing that the funds are in the owner's hands. This particular trust is designed to deal with the situations where the contract does not provide for the issuance of progress certificates as described in the Certificate Trust and cases where the payments made by the owner to the contractor total less than the amount ultimately certified to be due and owing at the date of substantial performance.

Draws Trust

This trust provides that the funds owing on account of the contract or subcontract, constitute a trust fund for the benefit of the subcontractors and any other persons who have supplied services or materials to the project.

Purchaser's Trust

This trust arises particularly in situations involving the construction of a new house. It is not uncommon for a developer/owner to conclude a sale before all the subtrades have completed their work and before they have been completely paid. Where it can be implied that the purchaser has given the trades assurances of payment or where they have purchased the house built in accordance with a sample or model, then that purchaser can be deemed the statutory owner and a trustee under the Act. This trust is not very common.

Vendor's Trust

When an owner sells their interest in a property, the proceeds received as a result of this sale are impressed with a trust for the benefit of the beneficiaries (contractor or sub-contractor).

What obligations are there?

Once in receipt of trust funds, the person cannot use those funds for their own benefit or for uses unrelated to the project until such time as all beneficiaries of the trust are paid. For instance, the person who has been paid cannot pay their overhead or pay themselves before paying the beneficiaries.

A contractor and a subcontractor have to follow these rules when they have received money on a construction project:

1. The trust funds shall be deposited into a bank account in the trustee's name. If there is more than one trustee, the funds shall be deposited into a bank account in all of the trustees' names.
2. The trustee shall maintain written records respecting the trust funds, detailing the amounts that are received into and paid out of the funds, any transfers made for the purposes of the trust, and any other prescribed information (there is no prescribed information as of the date of this guide).
3. If the person is a trustee of more than one trust under section 8, the trust funds may be deposited together into a single bank account, as long as the trustee maintains the records required under paragraph 2 separately in respect of each trust.

What funds are subject of the trust?

The Act only impresses with a trust, funds that constitute payment for materials and/or supply of improvements on land, not "chattels". In other words, anything that is detachable from the land is excluded from the Act. For example, proceeds of the sale of portable schoolrooms are not subject to the trust provisions as these schoolrooms were not affixed to the land.

Personal Liability of Officers, Directors or Controlling Minds

The Act contains special provisions that effectively "pierce the corporate veil" and hold the officers, directors and controlling minds of a corporation personally liable for any breach of trust committed by the corporation. This is a powerful tool that prevents persons from hiding behind a corporation and failing to make payments to the subcontractors/suppliers.

It is important to note that, for the defendant trustee contractor to be liable, intent is irrelevant. It is not necessary for the trust claimant to show any fraudulent activity on the part of the defendant. Merely standing by and allowing the corporation to commit a breach of trust can be sufficient for the individuals behind the corporation to be held liable.

PROMPT PAYMENT

Why?

The changes to the new *Act* were almost all predicated on tightening cash flow. The Canadian construction industry has seen a dangerous trend of aged receivables creeping into 70 day + territory, notwithstanding that most construction contracts speak to payments on net 30-day terms.

49 of 50 states in the United States and the US federal Government have some form of prompt payment legislation or regime and many have had so since the 1980's. We are borrowing from the American regime with our own prompt payment system tailored for Ontario.

The General Rule

The "Rule of 7" applies. All milestones for prompt payment are based on a seven-day week.

The General Rule is that there must be payment by owner to contractor in 28 days and then to subcontractor, 7 days later, then to sub subcontractors/suppliers 7 days later, payments being made on each subsequent seven-day interval down along the contractual chain.

These payment milestones are all triggered by a "proper invoice".

Proper Invoice

A "proper invoice" will require the following components:

- a. Name and address of contractor;
- b. Invoice date;
- c. Contract No. or other authorization for materials delivered and/or services performed;
- d. Shipping and payment terms;
- e. Name, title, telephone # and complete mailing address of the responsible person to whom payment is to be sent;
- f. Any other substantiating documentation/information required by the contract (statutory declaration, WSIB clearance certificate, etc).

Giving of proper invoices

The operative section of the new *Construction Act* provides:

6.2(1) Proper invoices shall be given to an owner on a monthly basis, unless the contract provides otherwise.

Restriction on conditions

(2) A provision in a contract that makes the giving of a proper invoice conditional on the prior certification of a payment certifier or on the owner's prior approval is of no force or effect.

Same

(3) For greater certainty, subsection (2) has no application to a provision in a contract that provides for the certification of a payment certifier or the owner's approval after a proper invoice is given.

Let's break these subsections down.

Unless the parties agree otherwise, proper invoices are to be submitted monthly. You will need to review the payment terms of whatever work you may be bidding on to determine whether or not you need to protect yourself qualifying your bid to ensure that you are being paid on a monthly basis.

Each "payer" on a proper invoice continues to have right to set off outstanding debts, claims or damages in relation to the contract at issue.

Please remember that the flow of funds does not always continue down a contractual chain on a construction project and that sometimes a set off, or back charge or withholding can be initiated by any party along the contractual chain.

As between an owner and a contractor, if the owner disputes a proper invoice, the owner may refuse to pay some or all of the amount payable under the proper invoice if owner gives the contractor notice of non-payment no later than 14 days after receiving the proper invoice from the contractor. The notice must:

1. Specify the amount of proper invoice that they are not paying; and
2. Detail the reason for non-payment.

As we know from the General Rule, if a contractor receives full payment of a proper invoice within 28 days, contractor shall pay each subcontractor who supplied services/materials under a subcontract no later than 7 days after receiving payment.

However, if a contractor does not receive full payment of a proper invoice within 28 days, the contractor shall pay each subcontractor no later than 35 days after giving proper invoice to the owner unless the contractor has delivered a notice of non-payment within the requisite time.

That notice must:

1. State that some, or all, of the amount payable to the subcontractor will not be paid within the specified time due to non-payment of the owner.
2. Specifying the amount that will not be paid.
3. Provide an undertaking to refer the matter to adjudication no later than 21 days after giving notice to the Subcontractor.
4. Provide a copy of any notice received from the owner regarding non-payment.

If a contractor disputes some or all of the amounts the subcontractor is claiming, the contractor may refuse to pay if the contractor gives a notice of non-payment within

1. 7 days of receiving a notice of non-payment from the owner.
2. 35 days of delivery of a “proper invoice” to the owner if no notice is given by the owner.

That notice must include:

1. The amount that is not being paid.
2. The reason for non-payment.

If contractor receives partial payment from owner, contractor must pay each subcontractor whose amounts were included in the proper invoice no later than 7 days after receiving payment.

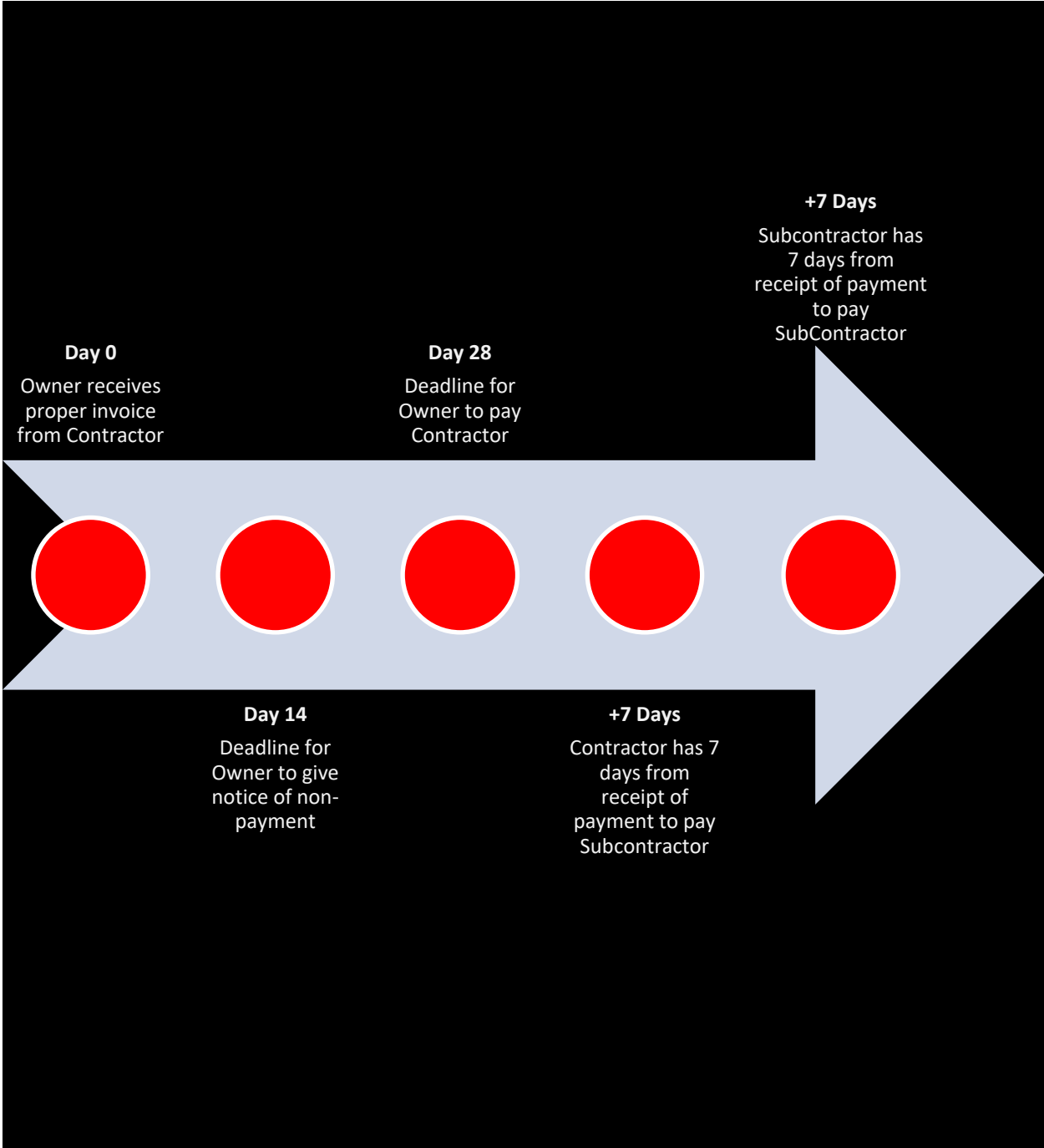
If the amount not paid by owner is specific to a subcontractor or subcontract doors, other subcontractors, the remaining subcontractors are to be paid with any amounts paid by the owner.

The subcontractor(s) who are not implicated in the payment dispute shall be paid on a rateable basis.

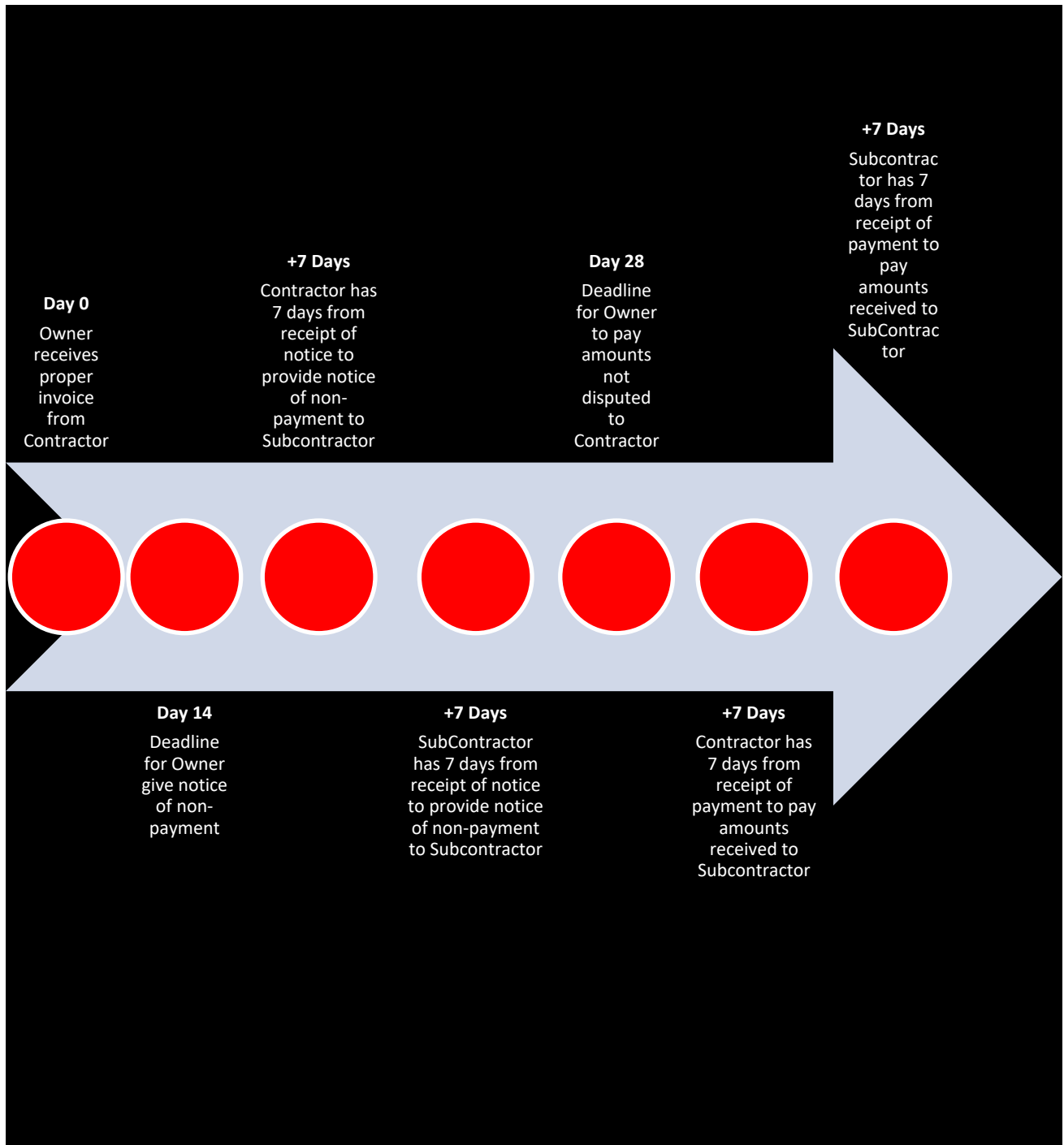
In any other situation, the Subcontractors should be paid on a prorata basis.

Hopefully, the following charts will provide valuable information on the proposed timelines for prompt payment:

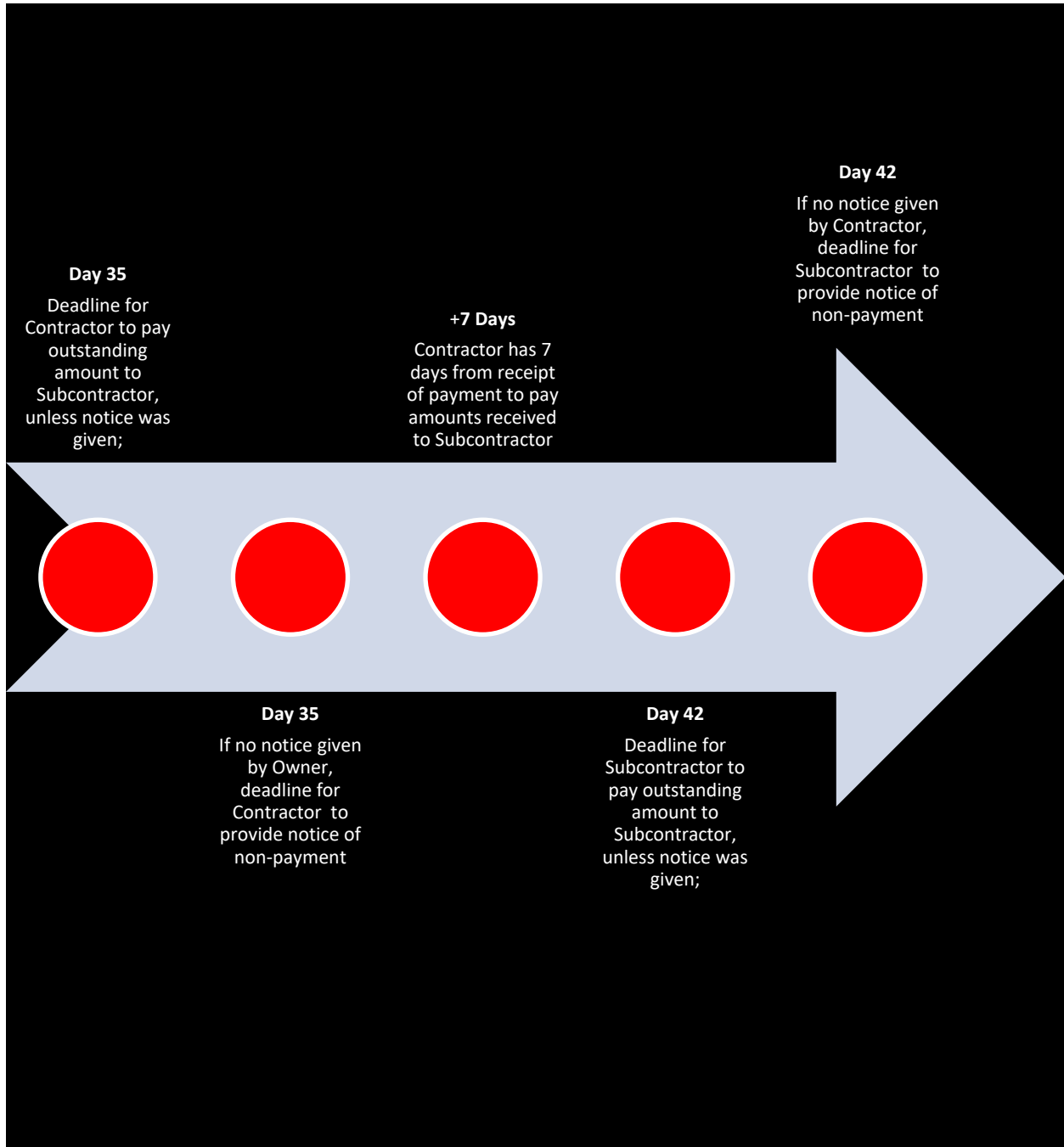
Full Payment



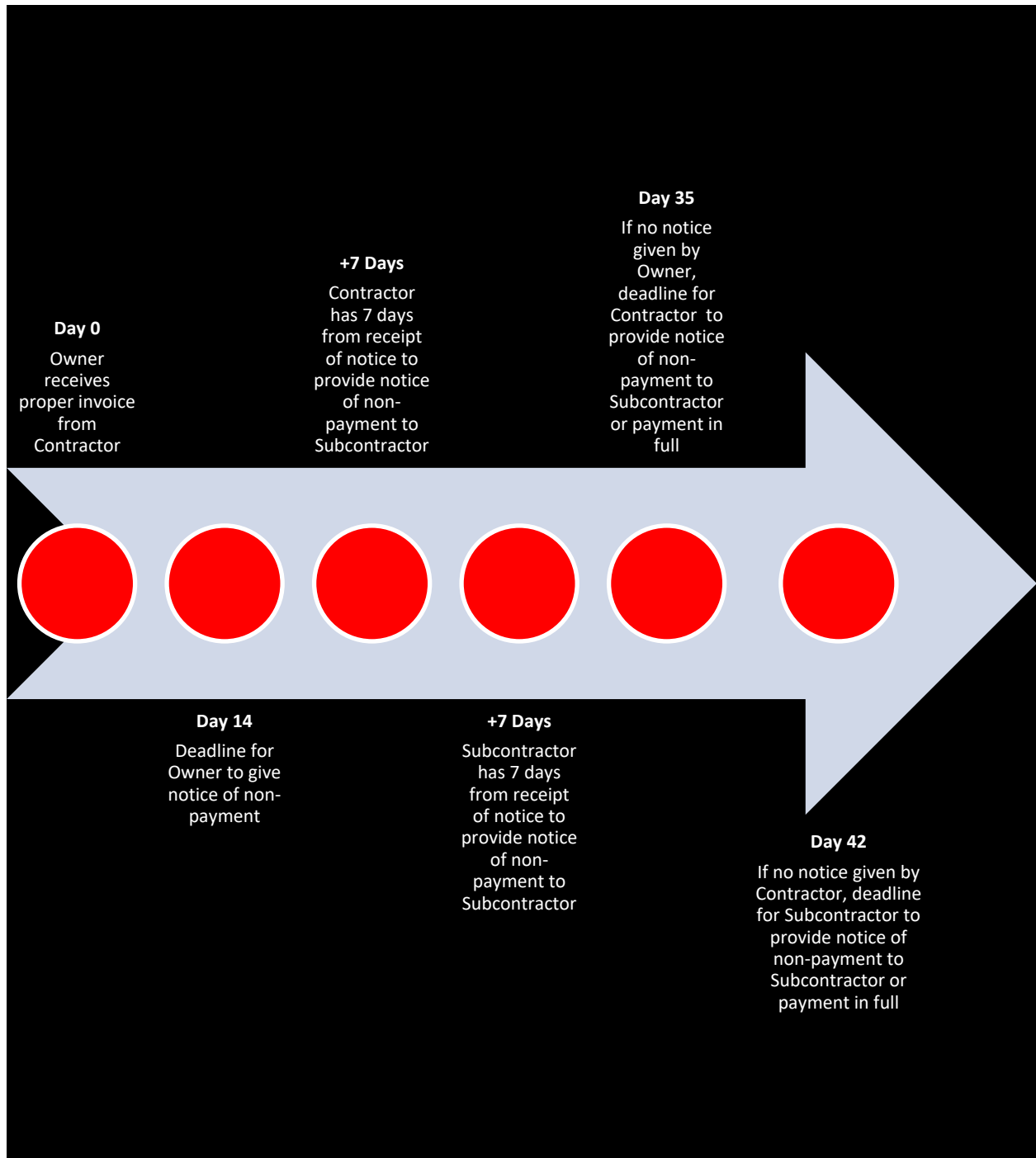
Partial Payment



Partial Payment- *continued*



Non-Payment



ADJUDICATION

What is adjudication?

Adjudication is a mechanism for resolving disputes arising under a construction contract without resorting to lengthy and expensive court proceedings. The process for an adjudication is intended to be simple and flexible. The objective is swift resolution of disputes and minimizing loss of profit and time involved in litigation.

Although the *Construction Act* as it is now called received Royal Assent on December 12, 2017, it has not been fully proclaimed in regard to the adjudication provisions. The adjudication provisions will be proclaimed and come into force on October 1, 2019 in order to allow sufficient time for the Authorized Nominating Authority to be established, to develop a regime for the certification of adjudicators, and to certify adjudicators. In short, this means that the adjudication provisions apply to contracts and in respect of subcontracts made under those contracts on or after October 1, 2019.

Adjudication may be new in this form to Ontario, but it is modelled over similar regimes being employed all over the world and in particular in the UK with great success over the last 30 years.

Can the parties agree that the adjudication regime does not apply to them?

Parties are not allowed to “contract out” of the adjudication regime. However, they can agree on provisions to be included in their contract and subcontract for adjudication as long as such provisions are consistent with the *Construction Act* and its regulations.

If the contract or subcontract do not address adjudication procedures, or if the adjudication procedures set out in the contract or subcontract do not comply with the requirements of the *Construction Act*, the adjudication is subject to the adjudication procedures set out in the *Construction Act* and in the regulations.

What types of disputes can be adjudicated?

A party to a contract or subcontract may refer to adjudication a dispute with the other party to the contract or subcontract any of the following matters:

- the valuation of services or materials provided under the contract/subcontract;
- payment under the contract/subcontract, including in respect of a change order, whether approved or not, or a proposed change order;
- disputes that are the subject of a notice of non-payment;
- amounts retained for set-off by trustee or for lien set-off;

- payment or non-payment of holdback; and
- any other matter that the parties to the adjudication agree to, or that may be prescribed.

Who can trigger an adjudication?

Only a party to a contract or subcontract can trigger an adjudication.

When can adjudication be commenced?

An adjudication may not be commenced if the notice of adjudication is given after the date the contract or subcontract is completed unless the parties to the adjudication agree otherwise.

A party may refer a matter to adjudication even if the matter is the subject of a court action or of an arbitration, unless the action or arbitration has been finally determined.

The thrust of adjudication is to deal with issues while they are live, while the project is ongoing.

Can an adjudication address multiple matters?

An adjudication may only address a single matter, unless the parties to the adjudication and the adjudicator agree otherwise.

Can multiple adjudications be consolidated?

If the same matter or related matters in respect of an improvement are the subject of disputes to be adjudicated in separate adjudications, the parties to each of the adjudications may agree to the adjudication of the disputes together by a single adjudicator as a consolidated adjudication. If the parties to each of the adjudications do not agree to consolidated adjudication, the contractor may, in accordance with the regulations, nevertheless require the consolidation of the adjudications.

When multiple adjudications are consolidated:

- the adjudicator may determine how the adjudication fee is to be apportioned between the parties;
- if the adjudicator obtains the assistance of a person (merchant, accountant, actuary, building contractor, architect, engineer or other person in such a way as the adjudicator considers fit), the adjudicator may fix the remuneration of the person and direct payment of the remuneration by any or all of the parties to the consolidated adjudication; and
- if the adjudicator determines that a party to the consolidated adjudication has acted in respect of the improvement in a manner that is frivolous, vexatious, an abuse of process or other than in good faith, the adjudicator may provide that the party be required to pay some or all of any party's (to the consolidated adjudication) costs, any part of the adjudication fee that would otherwise be payable by the other parties, or both.

Who can adjudicate a dispute?

An adjudication may only be conducted by an adjudicator listed in the registry established by the Authorized Nominating Authority (the “ANA”).

Adjudicators are not judicial officers. They are professionals in the construction industry such as accountants, engineers, architects, quantity surveyors, arbitrators, project managers or lawyers who have seven (7) or more years of relevant working experience in the construction industry. The adjudicators will be tasked to attempt to resolve disputes on construction projects. They will be expected to understand the construction process, how construction contracts works, and apply that knowledge in resolving disputes.

What is the Authorized Nominating Authority?

The ANA shall:

- develop and oversee programs for the training of persons as adjudicators;
- qualify persons who meet the prescribed requirements as adjudicators;
- establish and maintain a publically available registry of adjudicators;
- appoint an adjudicator when so requested by the parties;
- subject to regulations, set fees for the training and qualification of persons as adjudicators and for the appointment of adjudicators; and
- perform any other duties or powers as may be prescribed.

How is the adjudicator nominated?

When a dispute arises, the parties to the adjudication may agree to an adjudicator, or may request that the ANA appoint an adjudicator. A provision in a contract or subcontract that purports to name a person to act as an adjudicator in the event of an adjudication is unenforceable.

Appointing an adjudicator when the dispute arises allows the parties to select an adjudicator who is available at the time and suited to address the dispute at issue. It also avoids inequality of bargaining power that may exist at the outset of contractual negotiations.

How is an adjudication commenced?

A party to a contract or subcontract who wishes to refer a dispute to arbitration shall give the other party a written notice of adjudication that includes the following content:

- the names and addresses of the parties;

- the nature and a brief description of the dispute, including details respecting how and when it arose;
- the nature of the redress sought; and
- the name of the proposed adjudicator to conduct the adjudication.

What is a request for appointment?

If an adjudicator does not consent to conduct the adjudication within four (4) days after the notice of adjudication is given, the party who gave the notice shall request that the ANA appoint an adjudicator. The ANA shall appoint an adjudicator, subject to his or her prior consent, to conduct an adjudication no later than seven (7) days after receiving a request for the appointment.

Which documents shall be provided to the adjudicator?

No later than five (5) days after an adjudicator agrees or is appointed to conduct an adjudication, the party who gave the notice of adjudication shall give to the adjudicator a copy of the notice, together with:

- a copy of the contract or subcontract; and
- any documents the party intends to rely on during the adjudication.

What powers does the adjudicator have when conducting the adjudication?

The adjudicator may conduct the adjudication in the manner he or she determines appropriate in the circumstances. The adjudicator shall conduct the adjudication in an impartial manner.

In conducting an adjudication, an adjudicator may exercise the following powers and any other power of an adjudicator that may be specified in the contract or subcontract:

- issuing directions respecting the conduct of the adjudication;
- taking the initiative in ascertaining the relevant facts and law;
- drawing inferences based on the conduct of the parties to the adjudication;
- conducting (subject to the prior consent of the owner of the premises or of any other person who has the authority to exclude others from the premises) an on-site inspection of the improvement that is the subject of the contract or subcontract;

- obtaining the assistance of a merchant, account, actuary, building contractor, architect, engineer or other person in such a way as the adjudicator considers fit, as is reasonably necessary to enable him or her to determine better any matter of fact in question;
- making a determination in the adjudication; and
- any other power that may be prescribed.

How much time is an adjudication to take?

If the parties take the maximum times allotted to them to deliver documents and make decisions, adjudication is expected to take no more than 47 days. However, **it could be less than 47 days** if the initially named adjudicator is accepted right away and consents to the appointment, if the documents are delivered earlier than the five-day deadline, and if the adjudicator makes a determination of the matter that is the subject of the adjudication earlier than the deadlines under the *Construction Act*.

What timeframe follows the commencement of an adjudication?

An adjudicator shall make a determination of the matter that is the subject of an adjudication no later than thirty (30) days after receiving the following documents from the party who gave the notice of adjudication:

- a copy of the notice of adjudication;
- a copy of the contract or subcontract; and
- any documents the party intends to rely on during the adjudication.

However, the deadline for an adjudicator’s determination may be extended, at any time before its expiry and after giving the documents (see above) to the adjudicator:

- on the adjudicator’s request, with the written consent of the parties to the adjudication, for a period of no more than fourteen (14) days; or
- on the written agreement of the parties to the adjudication, subject to the adjudicator’s consent, for the period specified in the agreement.

A determination made by the adjudicator after the deadline (as may be extended) is of no force or effect.

Does the adjudicator have to provide written reasons?

Yes. The adjudicator’s determination has to be in writing and shall include reasons for the determination. The adjudicator’s determination and reasons are admissible as evidence in court.

Can a party terminate the adjudication?

At any time after the notice of adjudication is given and before the adjudicator makes his or her determination, the parties to the adjudication may agree to terminate the adjudication, on notice to the adjudicator and subject to the payment of the adjudicator's fee.

What happens when a party is required to pay?

A party who is required under the determination of an adjudicator to pay an amount to another person shall pay (subject to any requirement to retain a holdback under the *Construction Act*) the amount no later than ten (10) days after the determination has been communicated to the parties to the adjudication. The greater of interest between then contract interest rate and the *Courts of Justice Act* interest rate begins to accrue on an amount that is not paid when it is due to be paid.

What happens if a party does not obey the adjudicator's determination?

If an amount payable to a contractor or subcontractor under a determination is not paid by the party when it is due, the contractor or subcontractor may suspend further work under the contract or subcontract until the party pays the following amounts:

- the amount required to be paid under the determination;
- any interest accrued on that amount;
- any reasonable costs incurred by the contractor or subcontractor as a result of the suspension of the work; and
- any reasonable costs incurred by the contractor or subcontractor as a result of the resumption of work following the payment of the amounts referred to above.

This is very significant leverage for those not being paid. They can legitimately suspend further work. The thrust of the regime is to keep the funds flowing on the project as in pay now argue or reconsider later.

Who shall pay the adjudicator fee?

An adjudicator shall be paid a fee for conducting the adjudication, which shall be determined before the adjudication commences. The fee payable to the adjudicator is:

- the fee agreed to by the parties to the adjudication and the adjudicator; or
- if the parties and the adjudicator do not agree to a fee amount, the amount determined by the ANA on the adjudicator's request.

Unless an adjudicator determines that a party to the adjudication has acted in respect of the improvement in a manner that is frivolous, vexatious, an abuse of process or other that in good

faith (in which case the adjudicator may provide that the party be required to pay any part of the adjudicator fee), the parties shall split payment of the adjudicator fee equally.

If the adjudicator obtains the assistance of a person (merchant, accountant, actuary, building contractor, architect, engineer or other person in such a way as the adjudicator considers fit), the adjudicator may fix the remuneration of the person as is reasonable and proportionate to the dispute and direct payment of the remuneration by either or both of the parties to the adjudication.

Who bears the costs of an adjudication?

Each party to an adjudication shall bear its own legal fees and costs. However, the adjudicator has the ability to depart from that principle if a party to the adjudication has acted in respect of the improvement in a manner that is frivolous, vexatious, an abuse of process or other that in good faith (in which case the adjudicator may provide that the party be required to pay some or all of the other party's costs).

Are decisions binding?

The determination of a matter by an adjudicator is binding on the parties to the adjudication until a determination of the matter by a court, a determination of the matter by way of an arbitration, or a written agreement between the parties respecting the matter.

Nothing in the *Construction Act* restricts the authority of a court or of an arbitrator to consider the merits of a matter determined by an adjudicator.

Can a party challenge the determination of an adjudicator?

A party can challenge a determination of an adjudicator and try to set the determination aside on judicial review. However, an application for judicial review of a determination of an adjudicator may only be made with leave (permission) of the Divisional Court.

To obtain leave of the Divisional Court, a party shall file a motion for leave to bring an application for judicial review of a determination of an adjudicator no later than thirty (30) days after the determination is communicated to the parties. A motion for leave to bring an application for judicial review may be dismissed without reasons. No appeal lies from an order on a motion for leave to bring an application for judicial review.

An application for judicial review of a decision of an adjudicator does not operate as a stay of the operation of the determination unless the Divisional Court orders otherwise.

Can the determination of an adjudicator be set aside?

On an application for judicial review, the determination of an adjudicator may only be set aside if the applicant establishes one or more of the following grounds:

- the applicant participated in the adjudication while under a legal incapacity;
- the contract or subcontract is invalid or has ceased to exist;
- the determination was of a matter that may not be the subject of adjudication under the *Construction Act*, or of a matter entirely unrelated to the subject of the adjudication;
- the adjudication was conducted by someone other than an adjudicator;
- the procedures followed in the adjudication did not comply with the procedures to which the adjudication was subject under the *Construction Act*, and the failure to comply prejudiced the applicant's right to a fair adjudication;
- there is a reasonable apprehension of bias on the part of the adjudicator; and/or
- the determination was made as a result of fraud.

If the Divisional Court sets aside the determination of an adjudicator, the Court may require that any or all amounts paid in compliance with the determination be returned.

How are adjudicated decisions enforced?

A party to an adjudication may file a certified copy of the determination of an adjudicator with the court and, on filing, the determination is enforceable as if it were an order of the court. The party shall, no later than ten (10) days after filing the determination, notify the other party of the filing. The filing of the determination may not be made after the later of:

- the second anniversary of the communication of the determination to the parties; and
- if a party makes a motion for leave to bring an application for judicial review of a determination of an adjudicator, the second anniversary of the dismissal of the motion or, if the motion was not dismissed, the final determination of the application, if it did not result in the adjudicator's decision being set aside.

If a determination of an adjudicator requiring that an amount be paid to a contractor or subcontractor is filed with the court, any related requirement of the contractor or subcontractor, as the case may be, to make payments to a subcontractor is deferred pending the outcome of the enforcement.

Can the adjudicator be sued or compelled to give evidence?

No action or other proceeding shall be commenced against an adjudicator or his or her employees for an act done in good faith in the execution or intended execution of any duty or power under the *Construction Act* or regulations, or for any alleged neglect or default in the execution in good faith of that duty or power.

An adjudicator shall not be compelled to give evidence in any action or other proceeding in respect of a matter that was the subject of an adjudication that he or she conducted.

What is the status of regulations?

The adjudication regulations are necessary to implement the adjudication process established in the *Construction Act*. On February 9, 2018, the Attorney General released draft regulations. Stakeholders in the construction industry are invited to provide feedback regarding the draft regulations. The ministry will review the comments received from the industry and will make revisions to the proposed regulations, as necessary, on an ongoing basis. The proposed regulations will eventually be finalized, submitted for approval and filed. Of the draft regulations, we note the following anticipated highlights:

- An adjudicator registry will be publicly available online. The registry will include information such as the adjudicator's area of expertise for the purposes of adjudication and the geographical areas in which the adjudicator conducts adjudications;
- Adjudicators will be subject to a code of conduct. The code of conduct applicable to adjudicators will be publicly available online;
- Procedures and reasonable steps to ensure that adjudication is available to parties throughout Ontario will be developed;
- Educational materials respecting the adjudication process will be developed and will be publicly available online;
- An annual report containing information respecting adjudication in Ontario will be publicly available on the ANA's website. This will include information, *inter alia*: the number of adjudication conducted during the year and the area where the adjudications were conducted, the total amount and the average of the amounts claimed in all notices of adjudication given during the year, the total amount and the average of the amounts to be paid under adjudicators' determinations made during the year.

Even if the regulations are yet to be filed and that the Attorney General is considering a number of additional proposals related to the adjudication processes under the *Construction Act*, the draft regulations offer guidance as to what we can expect. The regulations (once adopted) will answer more questions so it is important to verify with your legal provider the application to your facts of the below questions and answers.

What are three important facts to retain about adjudication?

- A party cannot "contract out" of adjudication.
- When a party who is supposed to be paid under an adjudicator's determination is not paid, this party may legitimately suspend all further work until payment is received.
- The adjudication provisions will only start to apply to contracts and in respect of subcontracts made under those contracts on or after October 1, 2019.