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The Honourable Yasir Naqvi
Attorney General
Ministry of the Attorney General
720 Bay Street, 11th Floor
Toronto, Ontario M7A 2S9

Reference: Bill 142, Construction Lien Amendment Act, 2017

Dear Minister Naqvi:

Thank you for the opportunity to provide an early response in advance of second reading for Bill 142, Construction Lien Amendment Act, 2017.

We have offered our support for the "Striking the Balance" recommendations submitted by Bruce Reynolds and Sharon Vogel and for the policy direction and intent of Bill 142. We do however have concerns with specific drafting and unintended consequences of that drafting which is the focus of these comments.

On July 24, 2017, we met with Bruce Reynolds and Sharon Vogel and had a full and productive discussion. We have since amended our comments to include a number of issues that will diminish the effectiveness of this legislation if they are not addressed.

This is complex legislation requiring a diligent review in order to get it right. We have full confidence in the process and we will provide all the support required to aid the development of the most effective legislation possible.

In support of this process, we submit the following comments to you and the Ministry of the Attorney General for your consideration. We will also provide copies to Bruce Reynolds and Sharon Vogel.

OGCA Submission to the Ontario Ministry of the Attorney General

1. PROMPT PAYMENT (PART I.1):

a. **Non-payment of Holdback by Owner with or without notice.** As a general statement, there are several (likely inadvertent) inconsistencies between the time frames set out in the prompt payment section and elsewhere in the Act. For example, while s. 6.4(5) contemplates a right to suspend payment if an ordinary monthly invoice is unpaid, that section is inapplicable to the obligation to pay holdback, which is addressed in section 27.

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S. 27.1 requires a payer to make payment of holdback no later than 40 days following substantial performance unless the payer provides notice down the payment chain. If an owner provides notice to a contractor on the 40th day, a contractor would not have an opportunity to provide a corresponding notice to its subcontractors. Similarly, an owner may neglect to provide notice yet still fail to pay a contractor. In both cases, the Act does not provide an opportunity for a contractor to provide the required notice, effectively requiring a contractor to pay holdback without receiving the funds from an owner. This is at odds with the prompt payment provisions of the Act, which permit a contractor to suspend payment in the event that an owner fails to make payment.

Proposed Resolution: The deadline following substantial performance for a contractor to pay holdback down the payment chain should be 47 days. This will permit a contractor to provide notice to subcontractors should an owner provide notice of non-payment or fail to pay holdback as prescribed. In the alternative, the time limit in s. 27.1 for a contractor to give notice of non-payment should be extended to five days beyond the date that it receives notice from the owner. As a further alternative, the payment suspension mechanism in section 6.4(5) should be reproduced or referred in section 27.1 (subject to modification as recommended in item 1.d below).

b. **Non-Payment of Adjudication Determination**: The payment suspension right in the prompt payment section is not built into the adjudication section. S. 13.19 requires a party to make payment within 10 days of an adjudication determination. In a "back to back" adjudication, if an owner does not make a required adjudication payment, there is no payment suspension right which allows a contractor to defer payment down the payment chain. This is at odds with other provisions of the Act, which permit a contractor to suspend payment in the event that an owner fails to make payment.

Proposed Resolution: Modify the adjudication section s. 13.19 by making it subject to flow down provisions similar to 6.4 (8) and extend the deadline for a contractor to pay an adjudication determination to 15 days to permit a contractor to provide notice to subcontractors should an owner fail to make payment as directed further to an adjudication determination. In addition, in a "back to back" scenario the payment obligation of the party in the middle should not arise until it receives funds from up the chain.

c. **Owner Insolvency Risk**: It is our understanding from the Report that the intention of the Act is to allow contractual "pay when/if paid" provisions to continue to be enforceable. However, the mechanics of the Act allow for a plausible argument that such provisions are invalid. The argument would be that (a) per s. 4 every contract is amended to conform with the Act, (b) the Act imposes a strict payment terms and (c) the Act contemplates pay when paid only when the contractor meets all the requirements of 6.4(5). It is critical that parties remain free to contract as to pay when/if paid.

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Proposed Resolution: Include an express statement that the Act does not prohibit pay when/if paid terms within subcontracts of any tier.

d. **Prerequisite to Access Payment Suspension:** s. 6.4(5) requires a contractor, as a condition to access payment suspension, to provide an undertaking to begin adjudication within 14 days after giving notice of non-payment to a subcontractor. Following the release of the Striking the Balance Report, the industry understood from the information sessions that payment suspension could be accessed by diligently following the dispute resolution process outlined in a contract and that there would not be a mandated requirement to (prematurely) escalate a dispute. The stricter requirement to adjudicate would effectively override any dispute resolution procedures in both prime contracts and subcontracts. These procedures vary as a function of the size, nature and complexity of a project and the industry would not be well served by imposing a simplistic and one-size-fits-all dispute resolution procedure on all projects. The issue is particularly concerning in the case of insolvency where there has been a stay of proceedings and the contractor is unable to persuade the court to lift the stay to commence an adjudication, which would have the unintended consequence of preventing the contractor from accessing the statutory right to suspend payment.

Proposed Resolution: Section 6.4(5)(iii) should be amended to expand the options the contractor has to pursue payment to include not only (i) adjudication, but also (ii) initiating lien proceedings, (iii) initiating a civil action, and (iv) diligently pursuing the dispute resolution mechanism in the contract, provided that should the contractor invoke option (iv), should payment remain outstanding for 120 days, the contractor would be required to commence one of the more formal proceedings (options (i) through (iii)).

e. **Proper Invoice:** It is a common occurrence that a contractor and its subcontractors amicably agree with an owner to revise a monthly invoice following review and discussions with an owner's consultants. Such a revision to an invoice does not typically extend the timelines for the owner to make payment. This is a practical and healthy process. The Act does not contemplate such a process and encourages a less collaborative and potentially confrontational approach.

Proposed Resolution: With the consent of both the owner and contractor, permit a revised invoice to be submitted, backdated to the date of the original proper invoice.

2. ADJUDICATION (Part II.1):

a. Back to Back Adjudication: The "Striking the Balance" report recommended that the Act should include "back to back" adjudication as between a subcontractor and contractor in the event of a dispute with an owner. The Act, however, only provides for "consecutive" adjudication (s. 13.8(1)).

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It is critical to all involved parties that an adjudicator's determination in all related adjudications be made based on the same facts and presentations and be consistent. This consistency could be best achieved if "back to back" adjudications were undertaken concurrently and an adjudicator's determination addressed payment responsibilities of all parties.

Further, it is common that a dispute with an owner concerning scope of work would involve several subtrades. In many cases, there is essentially no dispute between the contractor and the subcontractor and the determination essentially flows from the owner through to the subcontractor. It would be imprudent for a contractor to adjudicate with an owner and not invoke consecutive adjudication with its subcontractors. To do so would expose the contractor to the risk that a subcontractor who was not satisfied with the adjudication determination between the owner and contractor which would flow down to the subcontractor, could elect to adjudicate with the contractor. This adjudication would likely consider different facts and presentations than the owner/contractor adjudication and could generate a different determination.

As a practical matter, it would also not be in the public interest to significantly disrupt the proper execution of projects by compelling key project management personnel to spend significant time away from the project to participate in multiple consecutive proceedings on the same issue. The party in the middle of a consecutive adjudication will also be forced to incur double the costs of the other parties, simply because it is in the center of the payment chain. This is an unfair result, particularly in circumstances where the consecutive adjudications relate to a pass-through claim (for example, between a subcontractor and owner, where the contractor is caught in the middle). A consecutive adjudication regime would require multiple individual adjudications that would be more efficiently and fairly addressed by allowing back to back disputes in a single adjudication or, at a minimum, concurrent adjudications.

> Proposed Resolution: Section 13.8(1) should be modified to allow parties the option of including the party above and/or parties below in the payment chain in a single adjudication proceeding, or if the drafters believe that there should be separate proceedings, at a minimum "consecutively" should be modified to say "consecutively or concurrently". Section 13.8(2) should be revised in the same manner as Section 13.8(1) to allow contractors to require a single adjudication with an owner and one or more subcontractors, or to allow concurrent adjudications.

Further, we understand that where there are consecutive adjudications, the intention is that the adjudicator would not render his/her decision until the completion of the final adjudication (in order to avoid inconsistent decisions). If that is the intention, we would suggest that s. 13.8 and or s. 13.13 be modified to expressly state that term.

3. TRUST PROVISION (Section 8.1):

Depending on the details surrounding the implementation of "NY style" bookkeeping, the OGCA has significant concerns about the complexity and effort required to comply. The OGCA and its membership represent the general contracting industry. We have practical expertise which would be relevant to the development of supporting regulations. Accordingly, we request that the OGCA be given the opportunity to provide input into the development of the related regulations.

4. AFP PROJECTS (Section 1.1): For AFP projects, section 1.1(2) states that the Crown, municipalities and BPSOs (each an "Authority") are not subject to the prompt payment and adjudication provisions of the Act. This exclusion will cause significant problems on AFP projects. We anticipate that lenders might see this exemption as a break in the chain that will create increased risk for PCo.

For example, if an authority is late making a capital payment, PCo would be unable to comply with its prompt payment obligations (and in extreme cases the non-payment could trigger an insolvency). By making PCo the "owner" and removing the real payor from the reach of the Act, PCo has a statutory obligation to pay on a fixed timeline but not a statutory right to receive payment on a fixed timeline. Further, because the Authority is not an "owner" for purposes of the Act, PCo is also not able to invoke the payment suspension provisions of section 6.4 (even if the Contractor and/or Subcontractors have invoked such rights due to a non-payment by the Authority).

Similarly, if the adjudication provisions do not apply to the Authority, there is strong potential for a misalignment between the procedures to determine entitlement to a Change or to settle a dispute, which would effectively strand risk at the PCo level, making financing a project very challenging and likely more expensive for taxpayers. Although the adjudication section provides for "back to back" adjudications, in this case PCo has no ability to bring the Authority into the adjudication. A Contractor could win an adjudication award against PCo, but PCo would have no right to secure a back to back award against the Authority, thus creating a stranded risk. For example, an adjudicator could interpret the technical specifications a certain way, but that interpretation would not be binding on the Authority. This will lead to confusion regarding the scope of work that the Contractor is required to deliver to PCo as opposed to the scope of work that PCo must deliver to the Authority.

Proposed Resolution: Do not refer to Sections 1.1(2)(1) and 1.1(2)(2) in Section 1.1(3). AFP projects must be "all in" or "all out". All participants in AFP projects, including the Authority, must be subject to the prompt payment and adjudication provisions of the Act. The only alternative is to exclude AFP projects, including all participants – the Authority, PCo, contractors, etc. - from those provisions to avoid these issues.

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5. MISCELLANEOUS ISSUES:

a. **Milestone Payments:** It is a common scenario in large projects (AFPs, EPCs, etc.) that the payment scheme between owner and contractor is entirely disconnected from that between contractor and subcontractors. For example, the owner (or Project Co) might pay the contractor monthly, while the contractor pays its designer on milestones such that the contractor may receive several payments from the owner before it makes the first payment to a designer (this is done as a risk management measure). That system would be problematic under sections 6.4(1-3) and 6.5(1-3) of the Act. For example, section 6.4(1) would require the contractor to "pay each subcontractor who supplies services…that were included in the proper invoice", which would mean that since the contractor received payment from the owner, some portion of which was attributable to work performed by the designer, the contractor would be statutorily compelled to make a payment to the designer, notwithstanding that the designer has not yet completed its milestone.

> Proposed Resolution: Sections 6.4(1-3) and 6.5(1-3) should not apply to contracts and subcontracts, respectively, to the extent that those contracts or subcontracts provide for milestone payments.

b. **Setoff:** The OGCA understands that the impetus for eliminating the right of setoff in the Act was to protect and make funds available to lower tier participants in the industry in the event of a contractor or subcontractor insolvency. In our experience, however, eliminating the right of setoff will have the opposite effect. In the case of a subcontractor insolvency affecting multiple projects of a contractor, the funds setoff from one project are typically used to pay claims related to another project from 2nd tier subcontractors and suppliers who were not paid by the failed subcontractor. Eliminating the right of setoff would likely force the contractor to pay these funds to a receiver and the primary beneficiaries would be secured creditors such as banks or the CRA, while unpaid lower tier subcontractors (that would otherwise have been paid under the current state of the law) would be limited to claim against the holdback fund.

> Proposed Resolution: Do not restrict the right of setoff that currently exists in law. This can be accomplished by not amending sections 12 and 17(3) of the Lien Act, such that the original language in the Lien Act, "whether or not related to the improvement", remains unaltered.

c. **Adjudicator Support Expenses:** Under section 13.12(1)(5) and 13.12(3), an adjudicator has broad powers to hire consultants with no reference to proportionality or reasonableness.

> Proposed Resolution: Condition the power of an adjudicator to retain consultants and advisors in section 13.12(1)(5) subject to proportionality and reasonableness.

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d. **Transition:** Industry participants are in a very difficult position if, during the transition period, the Act applies to some participants in a project and not others. For example Section 13.23 creates the scenario where adjudication could apply to subcontracts but not the prime contract

> *13.23 This Part applies in respect of contracts and subcontracts entered into on or after the day subsection 11 (1) of the Construction Lien Amendment Act, 2017 comes into force*

Proposed Resolution: The Act should apply only to Prime Contracts (the "contract" as defined by the Act) executed after the Construction Act comes into force, and all subcontracts entered into in relation to those Prime Contracts.

e. **Bonds:** There has been discussion about the bond form that will be prescribed under the Act and we anticipate that the form will be included in the regulations. We are supportive of a bond which ensures that 2nd tier subcontracts can call on the bond in the event of a contractor insolvency, but not a bond which permits 2nd tier subcontractors to access the bond in the event of a subcontractor insolvency. Unlike federal projects, 2nd tier subcontractors subject to the Construction Act have the benefit of lien rights. As well, permitting 2nd tier subs to access the GC's bond because of a subcontractor failure would encourage irresponsible credit practices amongst suppliers.

Proposed Resolution: The prescribed bond form should mirror current federal broad form bond formats which do not provide relief in excess of what would be available if the lien act applied.

f. **Definition of Day:** There is evidence in the UK of abuse of the timelines for adjudication which are defined in calendar days permitting aggressive parties to make submissions around holiday periods to frustrate the response of the opposing parties.

Proposed Resolution: The Act should clarify that short deadlines specified in the Act refer to business days instead of calendar days. Longer timelines would not need to change. We therefore propose adding the following clause into the Act:

> Where the time limited by this Act for the doing of any thing is less than or equal to ten (10) days, then only days that are not holidays shall be counted when calculating such time period.

Thank you for your consideration of these issues. We welcome any opportunity to meet with the Ministry of the Attorney General to review these submissions and discuss the issues and our proposed resolutions.

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OGCA not only supports the legislative process but will work with our members and the industry to promote the reforms and educate general contractors. This is the most significant legislation to impact the construction industry in many years and it is vital that we do everything possible to make sure it is effective and understood.

Please let me know if we can be of further assistance.

Yours sincerely,
ONTARIO GENERAL CONTRACTORS ASSOCIATION

Clive Thurston
President