

Construction Lien Act Review Consultation Meeting Summary
Enbridge Gas Distribution Inc.
December 4, 2015 (9:00 a.m. to 11:00 a.m.)

Attendees: Michelle Cook, David Donovan, Bruce Reynolds, Sharon Vogel

Sheryl Cornish, Counsel at the Ministry of the Attorney General, attended the meeting to record a summary.

For the introduction provided by the Review, please see document titled BLG Consultation Introduction.

1. General Overview of Enbridge Gas Distribution Inc.

Enbridge Gas Distribution Inc. (“Enbridge”) wants to make sure that they remain on the stakeholder list. It had been anticipated that more would self-identify but that has not been the case. The Review has not met with any other utilities.

Enbridge comes from the gas distribution side, which serves about 2.1 million customers. This is over half of natural gas customers in Ontario. It operates in the area between public and private owner groups. The key issues are similar to publicly owned electric utilities because Enbridge is a large utility. It works closely with municipalities, electric utilities, and anyone else who puts pipe in the ground.

Enbridge is a member of the Ontario Energy Association (“OEA”), which represents all utilities in the province. The OEA participated in the Enbridge submission, but did not voice a position on behalf of the OEA because there has not been enough interest from the members. They have elected to be an observer in the process.

When Bill 69 was introduced, it was the first time Enbridge saw these issues raised. They thought Bill 69 would fail, but it went to Standing Committee and there was a lot of discussion. There was internal discussion about whether to voice concerns about the Bill. Enbridge decided to make a written submission to the Committee.

2. Ontario Energy Board Regulation of Construction Projects

Enbridge is heavily regulated by the Ontario Energy Board (“OEB”) and its related legislation. All major construction projects go before the OEB. Enbridge is required to file an application for leave to construct prior to any construction. It wants to ensure that the flexibility that it has from the OEB survives the Review.

Enbridge understands the need to reform the legislation because it is outdated. There are things that are important for the flexibility of Enbridge’s projects. It proposes projects and the OEB rigorously goes through the plan to ensure that everything is done properly and in the public interest. Part VI of the *Ontario Energy Board Act, 1998* deals with construction, and section 96 talks about the OEB giving an order if it is in the public interest. A certain threshold has to be met and there is a need to meet a series of requirements.

Enbridge must show prudence as part of the public interest test. This is important when negotiating a contract and trying to get a project approved, because they need to show that they are getting value for money. Their expenditures are paid for by the ratepayers and they must meet prudence tests.

When it comes to prudence, the OEB has oversight regarding the decisions Enbridge is making. The Board can reject the project if Enbridge is not getting market friendly terms. There have been requests for proposals ("RFP") where Enbridge has received a lot of OEB oversight.

If Enbridge has not spent money properly, they can have a disallowance and the costs cannot be passed on to ratepayers. If there are cost overruns, Enbridge may get a disallowance. This would have to be paid by the shareholders. The OEB reviews it on a project-by-project basis. If there is a cost overrun, the OEB can disallow it.

3. Release of the Holdback

Enbridge is tightly regulated and they are required to lower costs so that they are under inflation. They are under incentive regulation. This is a new system, which is currently in its second term. When Bill 69 came up, they talked about getting rid of holdbacks. In order to make sure that Enbridge gets value for money and people to finish the job, it relies heavily on holdbacks.

On facilities contracts there are two additional holdbacks. One is for manuals and documentation, which is calculated based on how much it would cost for Enbridge to create it themselves (usually it is about \$45,000 to \$50,000). The second is documents for LEED certification. This is required because when clients build they are very energy conscious (this is less than \$100,000). Enbridge did not always have the LEED holdback, but they were not getting the documents promptly so the clients decided to put this holdback in. They now get it more promptly.

In terms of construction of pipeline, Enbridge has a holdback for final copies of all as-built construction drawings. They need to know where the infrastructure (pipelines) is so that they can present this information to the OEB.

Enbridge needs the holdbacks to keep the contractor's attention and to operate the system in a safe, responsible manner. If you are a contractor and you have subcontractors under you and the documents flow up to you, Enbridge needs everything promptly. This will depend on the size of the project.

Enbridge will check if it has a warranty and facilities holdback. One issue is that they do not want to pay until the project has been energized and it works.

Enbridge wants the flexibility to segment pipelines. It pays based on milestones depending on the size of the project. This was the problem with Bill 69.

Enbridge accepts phased release of the holdback if it is set out in the contract, rather than required by statute. Every project can be different in terms of the size, scope, and scale. Different pricing and payment mechanisms are required.

On the construction side, there are a lot of issues to consider, including political issues, geo-tech issues, and permits. Enbridge would prefer freedom to contract. Its contractors are very large and sophisticated.

4. Bidder Qualification

Enbridge has a pre-qualification process for contractors, which is important to monitor contractor performance. The goal is to have qualified contractors complete the construction. When Enbridge does an RFP, they do a pre-qualification process upfront. The contractor must be a member of ISNetwork, which is a storage house for IHNS information. They must answer a questionnaire and give them a clearance certificate and CAD 7. Using criteria determined by Enbridge, ISNetwork will develop a score. The contractor needs a specific score to do certain types work. There are approvals and mitigation if the contractor does not have the required score.

5. Financial Disclosure

Enbridge has 40 pages of supplementary provisions to the CCDC for facilities work (buildings that people will be in). There is a different contract for pipeline work. For smaller jobs, they have a mini CCDC. They also have a general services contract and will create a schedule to that if there is a low dollar value.

Enbridge is concerned about additional financial disclosure beyond what is publicly available. The financial disclosure provisions are always removed from the CCDC. Enbridge is publicly traded and has certain *Securities Act* requirements. All projects are on the OEB website, which includes all submissions, intervenors, and comments from stakeholders.

The Review is hearing that stakeholders want disclosure because they want to know that people they contract with have the money to pay them, the project is approved and it will go ahead. If there are delays and they are asked to hold their prices, this puts them in a difficult position, especially when they have to buy materials. The prices that they are forced to pay may change and their suppliers will not hold their prices. If the project is not going to proceed and they are being asked to hold prices, or a private owner does not have the financing to pay, this is a concern. This varies based on the type of project.

6. Prompt Payment

The fundamental tension in the Review is freedom of contract and regulation. Enbridge is already regulated by the OEB and the Act. There are a few streams of regulation. It cannot contract out of the Act.

The Review is considering how far to move the line towards limiting the freedom of contract from what it is now in terms of accomplishing the policy goals of the Act. One of these goals is to provide a limited form of securitization for people down the chain in the construction pyramid. The Review has heard that from the owner's perspective it is about checks and balances and being a guardian of the public purse. From the contractor's perspective, they are waiting a long time to get paid. There are

repercussions for various sectors, including the contractors, subcontractors, trades, unions, union health benefit plans, pension plans, and workers.

Enbridge's financial payment system has many controls to meet regulatory requirements. It can take 60 days to get a cheque issued once it has gone through the approval process. This is from the date of receipt of invoice. They aim for 30 to 40 days, but based on anecdotal comments, cheques are going out in 60 days.

Prompt Payment Ontario ("PPO") did a trade contractors survey which involved a large number of trade contractors. The Review described the results from this survey generally.

Enbridge needs to make sure that it is getting good value for money. It cannot endorse a cheque until the architect says it is done to standard. The invoice comes in and it is scanned. Enbridge puts 40 days in its contracts, but it is taking longer to make payments.

Enbridge explained that typically its contractors do not lien because it always pays. The project is already approved by the OEB so it would be clear that the payment will be made. There may be a dispute over a change order, but it gets resolved based on a principled decision over who is responsible. Enbridge has a lot of long-term contractors that it uses regularly. The relationship is important; they must work together and trust each other.

Increasing Complexity of Projects and Payment Mechanisms

There are a few issues for the Review. One is that there are owners which the contractor community is not concerned about with respect to payment. There are other owner groups where the contractor community has significant concerns regarding payment. The other issue that has been put forward by proponents of prompt payment is that over time payment mechanisms have become more complicated. Decades ago, payments were within 30 days. Contracts and projects have become more sophisticated over the years.

The elements that go into the payment process also became more complex and the effect is that contractors sometimes submit defective progress payment requests. A lot of owners say that they regularly get defective progress requests and you should not start counting from the moment you get a defective request. The net effect is that a 30 day cycle has now become a 60 to 90 day cycle. Sometimes things have not been done or have not been done to standard. The parties discuss it and get it fixed and move on.

Enbridge will get back to the Review about the process for approving and send out payments to contractors.

The Review has heard that in this age of electronic banking it should not take so long to receive payment. Owner stakeholders have said processes can take time internally with things like personnel vacations, checks & balances and cheque runs.

Some stakeholders have also said that there are increasingly inventive ways of committing fraud that owners have to be careful of. There are financial controls for reviewing invoices and making sure that the work has been done before payment has been made.

The Charbonneau Report recently identified late payment as a contributor to corruption. Small and medium contractors in an economic crunch may seek alternative ways of financing and turn to organized crime. If you give one person the authority to pay or not pay, then inducements paid to that person can accelerate payment. This was part of the problem in Quebec.

Contractors say that elongation of payment traps working capital for a long period of time. They argue that the Review should recommend that the regulatory intrusion index be moved further towards the regulation end.

Enbridge suggested that it would be hard for contractors to submit a flawed progress draw because of the payment certification process. Enbridge has a robust compliance department and privacy officers. There is a lot of regulation and reporting requirements for Ontario businesses. They are constrained. Some things that frustrate contractors have come about as a result of other laws that owners have to comply with. It is unfair to say that owners are in conflict with legislation because of its financial system, which was created to comply with other statutory requirements.

Enbridge will provide a description of the regulatory constraints on the payment cycle, including the time it takes to process payments.

Owners have said that they want to pay. General contractors have ‘pay when paid’ provisions in their contracts. If a significant proportion of the work is being done by the subcontractors, they bear the burden. This is an issue that has been brought to the attention of the Review.

If you want people to be paid faster, there must be a way that you can validate and make sure the work is being done to standard. Enbridge has consultants for facilities work. They have a lot of inspectors, some of which are in-house. Testing is done and this can take time. If the owner is taking a risk on the timeline by paying promptly, it should not lose the holdback. If it is lost, the industry may have insurance or letters of credit to work around it. This may end up being more expensive. Generally, most owner stakeholders have raised the issue of maintaining the right of set-off for deficient work and keeping the holdback for potential set off.

7. Adjudication

In addition to the elongation of payment terms in the ordinary course and prompt payment, there is a separate issue that arises where you have “gridlock” on a project. On some projects, you can get into a major dispute and the litigation process is very time consuming. It can take years to resolve.

Stakeholders have promoted the concept of adjudication as a method to resolve such “gridlock”. It is a way for the owner and contractor to get to a resolution so that money

can flow. It is an interim binding decision. The parties agree on the adjudicator, or are assigned an adjudicator. The decision is enforceable as a judgment and the parties can go back and reopen the dispute at the end of the project. The Review has received very positive feedback on adjudication as a way to resolve disputes.

Enbridge does not encounter major disputes. This may be because it only deals with a limited number of contractors who have experience in this type of work. Enbridge works with its contractors to resolve disputes.

Enbridge will also send the Review supplemental information about the issue of registering Property Identification Numbers.

TOR01: 6161476