Construction Lien Act Review Consultation Meeting Summary
Surety Association of Canada

December 7, 2015 (1:00 p.m. to 3:00 p.m.)

Attendees: Raymond Bassett, Steven Ness, Bruce Reynolds, Sharon Vogel, James Little

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. Prompt Payment

Prompt Payment Ontario's Trade Contractor Survey

The Review explained the results of the PPO trade contractor survey generally.

The Surety Association of Canada ("SAC") noted that there is a culture of acceptance of late payment in the construction industry today. For example, many contracts say 30 days for payment, but often this is not observed. It could take 60 days to make payment.

SAC noted that when considering how to design a solution, the Review will have to consider the cost issue. It would be helpful to know the cost of the problem so you can compare it to the cost of the solution.

According to SAC, the surety industry is not well understood by the rest of the construction industry. It plays a pivotal role in the Ontario construction industry.

With respect to prompt payment, SAC was concerned with when the prompt payment advocates measure elongation of payment cycle and if they measure from submission of a progress draw. The Review noted that some public sector and broader public sector ("BPS") owner stakeholders have said that, frequently, the draw requests are incomplete or do not conform to the contract.

2. Freedom of Contract and Statutory Regulation

The Review has identified a spectrum where you have freedom of contract on one end, and regulation on the other. The Act constrains freedom of contract to some extent by regulating things like holdback, trust obligations, and special court processes. Some stakeholders suggest that prompt payment is a justified further movement towards regulation. Some owner stakeholders have stated it is an unacceptable intrusion in the freedom of contract.

The Review has also identified a tension between simplicity and complexity in solutions.

According to SAC, sometimes the way you name things changes the way you perceive them. Elongation could be characterized as the 'systematic breach of payment terms'.

Contract terms could be seen as ‘freedom from coercion’. The market may be seen, from some perspectives, as routinely accepting systemic breach of payment terms. Contracts set time frames. The challenge is what happens when parties breach the terms. Freedom of contract may be seen as including the freedom to enforce the contract without fear.

3. Payment Terms

The Review has heard from trade contractors that they are required pay suppliers the going rate for materials and there may be price fluctuations. SAC stated that the structural gap is that the trades may get squeezed because of where the gap sits. You would give relief to the trade by making the general contractor pay down. SAC’s suggestion was to try to avoid a solution that just shifts the marker up a little bit. The cost to the trade should not just be moved up to the general contractor.

Some contractor stakeholders have advised that if you are working on a dozen projects and you do not pay your supplier on one project, they will not give you material for any other project. This means the trades may be borrowing or breaching trust, according to SAC.

SAC explained that in order to achieve shorter payment timelines for the trades, you must do something about the payment from the owner to the general contractor. SAC suggested that this situation would theoretically not arise if you had no holdback concept. If you have money flow from the owner directly to everyone in the payment chain, you could deconstruct the model to try to come up with a solution. In the industrial context for example, the payment and approval process is integrated through technologies. You submit an application on the owner’s web application and there is no gap in the payment.

4. Release of the Holdback

Two of the issues the Review has heard about from stakeholders are the length of time it takes to process a monthly draw and the release of the holdback. SAC suggested that we need an approach that strikes the right balance without overly complicating things.

The Review has indicated to various stakeholders that when you talk about promptness of payment, you have the elongation of payment cycle issue, which relates to the monthly draw and the release of the holdback and you have the gridlock issue. There are proposals around trying to provide for earlier release of the holdback from some stakeholders (e.g. phasing, annual release, mandatory certification of completion of subcontracts).

According to SAC, you could think of the holdback as protection for the owner against seizure and sale of the land against people they do not know exist. The holdback is an absolute answer to the attack. If you are an owner and there are liens and you have the holdback, you can pay it into court. From that perspective, SAC suggested there is an argument that the Act is created primarily to protect the owner.

The Review has heard from some stakeholders that once substantial performance has occurred and 46 days have elapsed, the holdback is the protection against deficiencies. If you are a contractor or trade, you may think of it as your money and once the 46 days has passed, the money should come to you.

SAC noted that the obligation to make payments should primarily arise under the contract. The statute should modify this only on the basis of good public policy. The idea of mandatory release of the holdback is not workable in SAC's view because the obligation to pay becomes a statutory one. If it is no longer a holdback and there are no liens, if they have contractual right to retain an amount of money, they can retain it.

SAC explained that many contracts provide for additional holdbacks. If it is in the contract, they have built it into their price. What is happening appears to be commercial leveraging. The holdback is paid once the punch list is completed. There seems to be a significant element of systemic breach in the system. If you have 30 day payment terms and people are not paying, it means people are breaching these terms.

5. Adjudication and ADR

Another significant issue being considered by the Review is the inefficiency of dispute resolution. Some owner stakeholders have suggested that they do not want to have their contract commit them to mandatory mediation and they do not want the Act to require this. SAC suggested that mandatory mediation has a great track record of resolving disputes.

The Review noted that the Latham Report that was issued in the United Kingdom over 20 years ago, recommended the adopted of adjudication as a dispute resolution method. The Review discussed the concept of adjudication as it was developed in the UK.

SAC fully supports adjudication. If the parties agree to do something better, quicker or more efficient than what the Act currently provides for, there should be flexibility.

SAC explained that consideration should be given to whether adjudication would be absolutely binding or there is an ability to improve on the timelines in the Act. The other issue is to be sure that all parties related to the dispute are similarly bound (e.g. the prime contractor, subcontractors and supply contractors). If the process is binding on just in relation to the prime contract, the contractor may still be subject to the dispute resolution in the subcontract. It should be all or nothing. SAC suggested avoiding having parallel processes.

Some stakeholders have asked whether sureties should be included in the adjudication process. SAC explained that it makes sense contractually and from a policy perspective.

According to SAC, disputes under performance bonds almost invariably arise under construction contracts. There are some disputes that are unrelated to the contract. These kinds of issues would be adjudicated on an interim basis. If a dispute or issue does not impact other parties, they would not be part of that adjudication process.

Sureties answer for a breach by their principal. The surety product has the unique feature that they have recourse to their principals under their indemnity. SAC explained that if adjudication were to be adopted, the members of SAC may need to revise their agreements of indemnity to speak to adjudicated outcomes.

6. Miscellaneous

Certainty of Payment Through Bonds

In terms of possible remedies for the problem of prompt payment, the imposition of interest and the Bill 69 approach are two possible approaches but SAC explained that there is only one product that provides certainty of payment: the labour and material bond. It provides a dedicated pool of funds for trades and suppliers and provides the certainty of payment. It provides payment, whereas other remedies provide the incentive to pay. It puts money in the trades' hands.

With respect to collateralization, SAC explained that the owner runs a credit risk that they will not be paid in the end if they lose in adjudication. The performance bond could respond to claims of this type.

According to SAC, notice is about protection of claimants. There is a risk if the total claims may exceed the bond penalty. You could exhaust the bond penalty before the notice period is expired.

Some stakeholders have suggested that the lien period should be extended to 60, 90 or 120 days. One rationale put forward is that the labour and material notice period is longer so the lien period should be longer.

The SAC submission states that the trust provisions should be enhanced. It refers to the British Columbia model. The caveat is that there should not be an overly administrative scheme. The SAC has heard feedback that the BC model works well.