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Introduction

This paper sets out the basic principles relating to holdback obligations under the Ontario *Construction Lien Act*² and deals with some recent cases of note on issues relating to holdback, and claims against the holdback.

Part IV of the *Construction Lien Act* sets out the statutory provisions relating to holdback, and what can and cannot be done with the holdback in ss. 22 through 30. The opening section of the Part sets out the basic holdback.

“22(1) **Basic Holdback** - Each payer upon a contract or subcontract under which a lien may arise shall retain a holdback equal to 10 per cent of the price of the services or material as they are actually supplied under the contract or subcontract until all liens that may be claimed against the holdback have expired as provided in Part V, or have been satisfied, discharged or provided for under section 44 (payment into court).”³

The construction project is conceptually a pyramid of supply of services and materials by a contractor, and its subcontractors, to an owner. The owner⁴ is required to “holdback” from amounts paid to the contractor to ensure there is some amount left to

² RSO 1990, c.C.30, as amended.

³ s.22(1)

⁴ An “owner” is a statutorily defined term, and means any person, including the Crown, who has an interest in a premises, and at whose request and for whose benefit, or upon whose credit, or with whose privity or consent an improvement is made. There is case law expanding the meaning of owner, and note particularly the decision of the Ontario Court of Appeal in *Parkland Plumbing v. Minaki Lodge* 2006 CarswellOnt 2801. A mortgagee was found to be an owner for essentially making the important decisions in respect of a premises. A “request” for work to be done could be inferred from the totality of the circumstances.

those in the pyramid below if there is a payment problem. The claim to the holdback is preserved and perfected by the lien registered or given for that purpose.⁵ The liability of an owner to those lien claimants who have proved valid liens is also made personal⁶, and is not only a charge against the improvement to the premises.

Conceptually, holdback is that amount that an owner must maintain until all liens that arise as a charge against such holdback have been satisfied, discharged, or provided for (under s. 44). The basic holdback is 10% of the services and materials supplied to an improvement. It is common to refer to “notice holdback” as that “additional amount” of holdback required to be maintained in response to written notice of lien. “Holdback” is often notional as a payment certifier calculates, based on the approved progress draws of a contractor how much work has been done to date, and then deducts 10% of that amount. Further, construction lenders (usually mortgagees secured by a financing mortgage) similarly advance the amount certified as complete to date, less the 10% holdback.

It is fundamental to the concept of the *Construction Lien Act* that the holdback obligations are passed down in turn in the pyramid so that the financial burden of the holdback is shared. Also, those below in the chain enjoy priority to the claims for

⁵ As provided in the last section of Part III, “The lien of a person is a charge upon the holdbacks required to be retained by Part IV, and subject to subsection 17(3), any additional amount owed in relation to the improvement by a payer...”, s. 21.

⁶ s.23. The personal liability of an owner does not exceed the holdbacks required to be retained.

payment of those above; everyone of the same class shares rateably.⁷ Finally, there is usually only a notional holdback, and not actual cash, being held back at each level.⁸

The minute a claim for lien is registered or given, the payment process comes to a halt. If it does not there are serious consequences to the payer, and the owner, where written notice of lien is received. Those consequences are that the holdback obligation increases, and the owner is liable to pay twice ie. if he/ she pays in the face of a lien or written notice of lien not only does not discharge the holdback obligation it increases it. This is sometimes called the notice holdback. The operative section is:

“24(2) **Idem** - Where a payer has received written notice of a lien and has retained, in addition to the holdbacks required by this Part, an amount sufficient to satisfy the lien, the payer may, without jeopardy, make payment on a contract or subcontract up to 90 per cent of the price of the services and materials that have been supplied under that contract or subcontract, less the amount retained.”

A “written notice of lien” must identify the payer and the premises, the amount the person has not been paid and the amount that is owed to the person giving notice by the payer.⁹ Registering a lien is insufficient to trigger s.24 notice holdback as “receipt” is central to the increased holdback obligation. Always send a letter to the owner and the payer where your client is unpaid, or send the lien, as registered or given to both, once registered or given, to trigger this section.

⁷ s.80

⁸ A common misconception, notes one author Glaholt, D., *The 2010 Annotated Construction Lien Act*, p. 169.

⁹ *Andrew Paving v. Shell Canada Products* 1996 CarswellOnt 198.

The *Construction Lien Act* allows for the certification of subcontracts as complete to allow the early release of holdback under s.25. That section allows certification under s.33, and unlike s. 32, does not require publication of the certification in order for the section to operate to deem last supply. This allows for the early release of holdbacks in those involved in the initial stages of a large project. It is made on the contractor's request, and it is not clear what the consequences flow from a contractor declining the request.¹⁰

There has been, historically, conflicting case law as to how long the holdback must be retained. In other words where there is a dispute between the owner and contractor, many subcontractors are reluctant to wait for the determination of that dispute in order to receive their rateable share of the holdback. Arguably, holdback had to be quantified before any payment out of holdback could be ordered. Where the holdback could not be quantified funds could not be distributed.¹¹

A more nuanced concept arises in section 28 which allows a payer above to pay a person below in the chain, provided written notice of the payment is given, and that indirect payment shall be deemed to be a direct payment, but the holdback obligation (both basic and notice) are not reduced.¹²

¹⁰ One author takes the view, that subsection 32(2) also applies to set out the liability of the payment certifier who refuses to certify a subcontract complete.

¹¹ *Oram v. Toronto Transit Commission* (1997) 36 CLR (2d) 190 (Master)

¹² s.28.

More recently, subcontractors were able to have a substantial amount of holdback ordered to be released in *Urbacon Build Groups v. Corporation of the City of Guelph*.¹³ In *Urbacon*, a pre-trial motion was brought with leave to have the holdback determined. An improvement had been undertaken by Guelph and disputes arose about timeliness of completion and costs with the contractor Urbacon.

Important thematic principles underlying the holdback provisions of the *Construction Lien Act* were analyzed and articulated by Justice Corbett. The Basic Holdback was referred to as a “fund for the benefit of Urbacon’s subcontractors”.¹⁴ There was no agreement as to the validity of every lien and a Vetting Committee had been struck to establish the validity of the liens. It had not by then rendered its report. However, the evidence established at least “some of the subcontractors liens [would] be established”. Consequently, it was said to be known what the minimum holdback obligations were, and the minimum claims against it:

“In this case, the payment ought to be [the total of the uncontested subcontractor lien claims] divided by [the total of all subcontractor lien claims], all multiplied by the uncontested minimum holdback obligation. The remaining balance of the holdbacks would be remain for distribution rateably on the basis of claims subsequently proved on motion for summary judgment or at trial.”

Importantly, the dynamic quality of a section 39 request was recognized. An owner has a statutory obligation to advise of the “state of accounts between the owner

¹³ 2009 CanLII 72065 (Superior Court)

¹⁴ at para. 8.

and the contractor”.¹⁵ This leads to, in effect, the *Construction Lien Act* equivalent of a request to admit under the Ontario Rules of Civil Procedure. Except under the *Construction Lien Act* a statutory right to damages results from failure to provide the information. One of the statutory purposes of s.39 is to allow a lien claimant to obtain information to decide whether or not to prosecute or continue with a lien action.¹⁶

Justice Corbett in *Urbacon* distinguished between the Basic Holdback” and the “Additional Holdback” (commonly called Notice Holdback) as the latter is subject to s.17(3) whereas the former is not.¹⁷ Thus Justice Corbett was able to say that “the minimum liability to the subcontractors is the lesser of the Basic Holdback and the aggregate of all valid and subsisting contractor lien claims”.¹⁸ Further, despite interim payments, presumably under s. 28, the “the total amount of those [subcontractor lien] claims still exceeds the Basic Holdback, after taking into account [all] of Guelph’s payments”.¹⁹

The key finding was made during the summary and *ad hoc* process of appearances before Justice Corbett as the *Construction Lien Act* is supposed to be a

¹⁵ This includes more broadly, any payer be they “owner”, “contractor” or “subcontractor”, s. 39.

¹⁶ Further, s.39 is not time limited and enables a lien claimant to obtain information relevant to a breach of trust action.

¹⁷ at para. 24. A payer can set off against notice holdback, or additional holdback (equivalent concepts).

¹⁸ at para. 26

¹⁹ at para. 32

summary process as set out in s.67. Here, the dispute between the owner and contractor appeared to be heading to trial. The owner had stated that the minimum holdback was “approximately” “\$3,512,385.00 subject to set offs”. Then later the owner claimed the holdback was “roughly \$1 million.”

An issue arose as to evidence. Under the *Construction Lien Act*, the holdback obligation follows the “price of services or materials as they are actually supplied”. It is not uncommon for there to be disputes as to the validity of the certificates issued by the payment certifier although they are some evidence, perhaps persuasive evidence, of the price. Amounts sometimes turn out to be over certified, so this concern is real. In *Urbacon*, the owner made many arguments in an attempt to reduce the quantum of the basic holdback to a lesser “price... actually supplied”.

“The costs to complete the project are facts that may be used in assessing the value of the work done, However the measuring stick of the value is the proportion of the contract work completed and the contract price. The costs to complete are just one element of the evidentiary record that may be relevant to this issue, In this case, there is no evidence that the alleged additional cost to complete are evidence that the value of the work done is less than the certified value.”²⁰

Also, Justice Corbett found that the jurisdiction to order payment into court arose, in his view, not from the *Construction Lien Act*, *per se*, but by the Rules of Civil Procedure incorporated by reference, and Rule 20 in particular on summary judgment.²¹

²⁰ at para. 49.

²¹ at para 56.

However, a payer's broad right of set off in s.17(3) does not apply to reduce holdback obligations as set out in s.30, until all liens that may be claimed against that holdback have expired, been discharged, or provided for. And it never reduces the basic holdback obligation.

Finally, two last matters were disposed of. The fact that it was very unlikely the aggregate of valid and subsisting lien claims would be less than the Basic Holdback was enough to tip the balance and order the funds paid into court. In the unlikely event the Basic Holdback turned out to be less, those funds were preserved in court for the owner, pending summary judgment motions to prove the liens against it.²²

Recognizing this important holdback issue might be an interlocutory order, Justice Corbett extended the time to appeal it until 15 days after the disposition of any summary judgment motions for payment out of court, clearly final orders disposing of any particular subcontractor liens.²³

Sections 4 and 5 of the *Act* stipulates any agreement that states that the *Act* does not apply is void, and that every contract or subcontract relating to an improvement is deemed to be in conformity with the *Act*. The question of whether or not parties may contract out of holdback was discussed in *Myer Salit Steel Ltd. v. Mondiale Development Ltd.*²⁴ (May, 2009). Salit Steel, the supplier, had included in the contract a no-holdback

²² at para. 54.

²³ at para. 57-58.

²⁴ 2009 CanLII 9746 (ON S.C.). [*Salit Steel*].

on supply clause, but Mondiale, the developer, took the position that the no holdback provision was contrary to the *Act* and was therefore void. As a result, Mondiale held back more than \$500,000, which Salit Steel insisted was to be paid out under the contract.

Master Albert held that the provision was valid. In doing so she highlighted that the holdback obligation in the *Construction Lien Act* is designed to protect subcontractors below the supplier in the construction pyramid. As there were no subcontractors below Salit Steel there was no one in need of protection through lien rights.²⁵

Further, Master Albert held that the no-holdback clause did not eliminate a subcontractor's lien rights. For her, rather it recognized that there were no subcontractors who would be affected by such an agreement. Consequently, Mondiale was ordered to pay Salit Steel the holdback with interest, rather than waiting the usual 45 day period for claims against the holdback to expire.

²⁵ The Act does not actually "obligate" a payer to maintain the holdback for "every" supply to an improvement. What the Act says in Part IV, Holdbacks in s. 22 is that "each payer upon a contract or subcontractor *under which a lien may arise* shall retain a holdback. And then at s. 23(1) personal liability arises for holdbacks (on the owner only); and then at s. 24(1), payments can be made, without jeopardy, of up to 90% of the price of services or materials supplied.