

Ontario's New Prompt Payment Legislation – How It Will Work

Date: June 12, 2017

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As eagerly anticipated, the proposed changes to Ontario's *Construction Lien Act* were tabled in the Legislature on May 31. There will be many modifications to the existing provisions in the Act that should come into force in the spring of 2018.

There will also be two significant additions to the Act, Prompt Payment and Adjudication, which represent monumental changes to timing of payments on construction projects, and how disputes will be resolved.

This article provides an explanation of the prompt payment provisions. The next will focus on adjudication.

The *Construction Act*, as it will be known after the amendments come into force, will include a new part, Part I.1, titled "Prompt Payment". This Part will be made up of sections 6.1 to 6.8. Three of these sections set out 1) the owner's payment obligation down to a contractor, 2) the contractor's obligation down to its subcontractors, and 3) the subcontractors' obligations down to their sub-subcontractors. As an aside, neither the existing Act nor the proposed amendments use the term "sub-subcontractor", and everyone down the construction pyramid who does not have a contract with the owner will still be referred to as a "subcontractor", but this update will use the term "sub-subcontractor" for clarity.

It is important to draw a distinction between a "contractor" and what is colloquially known in the industry as a "general contractor". If someone has a contract with an owner, even if they would not consider themselves "general contractors", they are still a "contractor", and that designation carries with it the requirement to initiate adjudication on behalf of unpaid subcontractors, described below. Also, the prompt payment provisions will only apply to contracts entered into after the provisions come into force.

The Prompt Payment Trigger

The Prompt Payment timelines start with the delivery of a "proper invoice" from the contractor to the owner. To be considered a "proper invoice", among other things the invoice must include

the typical information: contractor's name and address, the amount payable, and contact info of the person to whom it is sent. It must also state the period during which services and materials were supplied, and the authority (including contractual authority) under which the services or materials were supplied. The invoice must also have a description, including quantity, of the services or materials that were supplied, and the payment terms. Further, the parties can agree via contract on additional requirements for a "proper invoice".

Unless the contract provides otherwise, proper invoices have to be given to the owner on a monthly basis. While an invoice can still be subject to review by a payment certifier, the Act will prohibit any contractual provisions that require approval of the certifier before an invoice is considered a "proper invoice".

Owner's Deadline to Pay Contractor

The owner must pay the contractor's proper invoice within 28 days of receipt. The owner can only defer payment if, within 14 days of receipt of the invoice, the owner gives a notice of dispute to the contractor. The notice must set out the amount that is not being paid, and all of the reasons for non-payment.

The notice will be in a prescribed form (the proposed regulations, which will include forms, have not yet been released). The new Act requires the dispute notice to include "all of the reasons for non-payment", suggesting that the owner might not be able to rely on any reasons for non-payment that are not set out in the notice, even if discovered after the fact.

The 14 day requirement is, to put it lightly, a very tight timeline for an owner to review and dispute an invoice. Whether billing is done on the statutorily implied monthly basis, or on a longer contractually-agreed term, owners must have in place a robust infrastructure to analyze invoices to ensure that the 14 day dispute window is not missed. Presumably, missing this 14 day window will be fatal to an owner's effort to resist payment based on the dispute, otherwise the time limit would be pointless.

Contractor's Deadlines to Pay Subcontractors

If funds are received by the owner, the contractor then has 7 days to pay the subcontractors who supplied services/materials that were included in the proper invoice sent to the owner.

If the owner chooses to pay only part of the proper invoice, and gave a notice of dispute to the contractor, but there are more than one subcontractors whose work was included in the invoice (and are thus owed money by the contractor), then the contractor pays the subcontractors under the following rules:

1. If the owner's notice indicates the dispute was with respect to work done by specific subcontractors, then the remaining (i.e. innocent) subcontractors get paid first, and any amount left over is paid to the impugned subcontractors on a pro-rated basis; or,

2. If the owner's notice does not indicate a problem with any specific subcontractor, then all subcontractors are paid on a pro-rated basis.

If the owner does not pay the contractor, or only pays part of the invoice, the prompt payment provision states that, subject to the below notice, the contractor still has to pay all subcontractors whose work was included in the invoice (even if subject to a dispute notice from the owner), and payment must be made within 35 days of the date the proper invoice went to the owner.

There are two types of notice (both in forms to be prescribed) that can be given by a contractor to subcontractors in order to avoid this payment obligation. Regardless of which notice the contractor gives, it has to be given within 7 days of receiving notice of non-payment from the owner. If no notice is received by the owner, the contractor must give notice before the expiry of the 35 day deadline to pay the subcontractor.

Unpaid contractors will have to make sure that one of the below notices is sent out, otherwise they will be funding the owner's non-payment out of their own pocket.

First, the contractor's notice to each subcontractor can simply state that the amount that is not being paid, and that it is not being paid because the contractor hasn't been paid by the owner. With this notice, the contractor must also undertake to commence an adjudication proceeding against the owner within 14 days.

This undertaking requirement is important. It means that while the contractor can download the effect of an owner failing to pay (and avoid funding the non-payment out of its own pocket), the contractor cannot download or avoid the obligation to pursue the owner for payment.

The second type of notice that a contractor can give subcontractors to avoid payment is a notice of dispute (similar to the notice that an owner can give to the contractor). In this notice, the contractor is required to set out the amount not being paid to the subcontractor, and, again, "all of the reasons for non-payment". With this notice, the contractor does not have to give an undertaking to pursue the owner.

Subcontractors Deadlines to Pay Sub-Subcontractors

Once a subcontractor is paid by the contractor, in full or in part, the subcontractor has 7 days to pay down to all sub-subcontractors whose work was included in the proper invoice.

Again, if the contractor pays only part of the amount owing to the subcontractor, gave a notice of dispute to the subcontractor, and if there are more than one sub-subcontractors owed money by the subcontractor, then the subcontractor pays the sub-subcontractors under the following rules:

1. If the contractor's notice indicated the dispute was with respect to work done by specific sub-subcontractors, then the remaining (i.e. innocent) sub-subcontractors get paid first, and any amount left over is paid to the impugned sub-subcontractors on a pro-rated basis; or

2. If the contractor's notice does not indicate a problem with any specific sub-subcontractor, then all sub-subcontractors are paid on a pro-rated basis.

If the contractor does not pay the subcontractor at all, or makes only a partial payment, the prompt payment provision states that the subcontractor still has to pay the sub-subcontractors whose work was included in the proper invoice (even if subject to a dispute), and those payments must be made within 42 days of the date the proper invoice went to the owner, unless the subcontractor gives notice down to the sub-subcontractors.

Again, the subcontractor can give one of two notices to the sub-subcontractor to avoid having to pay the sub-subcontractor out of its own pocket; notice of non-payment from the contractor, or notice of dispute (detailing all reasons for non-payment). Unlike the contractor's obligation, however, the subcontractor giving the notice of non-payment does not have to undertake to commence an adjudication proceeding against the contractor to collect.

Subcontractors' 42 day deadline to pay down to sub-subcontractors is triggered by the date on which the contractor gave the proper invoice to the owner. Because the subcontractor will not necessarily know when that was done, the Act will include a requirement that, on request of a subcontractor, the contractor must advise as to the date the proper invoice was given.

Finally, nothing in the prompt payment provisions affects the obligation of the contractor or subcontractor (or, as we've been calling them, sub-subcontractors, or anyone below them) to pay wages as provided for by statute, contract, or collective bargaining agreement.

Stay tuned for an update on the new "rough and ready" enforcement mechanism; Adjudication.