



ALBERTA CONSTRUCTION INDUSTRY COMMUNIQUÉ

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PAY WHEN PAID CLAUSES

Construction contracts often contain clauses designed to respond to the particularities of the industry. One such clause is the “paid when paid” clause found in many construction agreements. As its name suggests, a “paid when paid” clause is designed to prevent a general contractor from having to pay a sub-contractor until such time as the general contractor has been paid by the owner. In essence, these clauses attempt to transfer the risk of non-payment by the owner from the contractor to the sub-contractor; such that in the absence of such a clause, the contractor is responsible for payment to the subcontractor even though the contractor may not have been paid.

On one hand, contractors are keen on strict enforcement of “paid when paid” clauses. In their view, it seems unfair to have to pay, from their own pockets and through no fault of their own, for work that was performed by a sub-contractor for the benefit of an owner who fails to pay whether as a result of insolvency or otherwise. On the other hand, sub-contractors are keen on limiting the applicability of these types of clauses; as in their view, they have performed the work, kept up their side of the bargain and as a consequence feel that they thereby entitled to payment regardless of who signs the cheque.

As a result of these differences, both contractors and sub-contractors have been willing to litigate the applicability of these clauses. Yet, despite the number of cases, courts across Canada have been inconsistent in their interpretation of “paid when paid” clauses.

In 1988 Ontario’s highest court upheld the parties’ right to contract and as such enforced a “paid when paid” clause to the detriment of subcontractors. The court held that given the wording of the contract, the sub-contractor’s legal right to be paid did not arise until such time as the general contractor was paid by the owner (which may never occur). Alberta courts also followed Ontario in this line of reasoning.

Conversely, in a 1995 ruling, Nova Scotia’s highest court, tried to limit the effect of “paid when paid” clauses by ruling that sub-contractors have a legal right to be paid within a reasonable period of time following the completion of their work despite the fact that the general contractor has not, and may not be paid by the owner. The clause merely extended the time for the subcontractor to be paid. Since then, Prince Edward Island, Manitoba and British Columbia and Saskatchewan have followed the precedent established by Nova Scotia.

More recent decisions have not been helpful in bridging the gap between the two lines of thought, although they have attempted to delineate the language and form that is required to render these clauses valid. For example, in a 2001 Ontario decision, the Court was asked to interpret a “paid when paid clause” in relation an oral contract. More specifically, the parties had a written contract which contained a “paid when paid” clause the work under that contract had been completed but extra work was required which the parties agreed to orally. The

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owner then failed to pay, and the general contractor claimed that the oral agreement was an extension of the written contract. The court did not accept this argument. It concluded that the subcontractor was entitled to be paid for the extra work as this was outside of the scope of the original contract. The Court went on to note that not just any “paid when paid” clause will be binding as against a subcontractor and therefore clear and unambiguous language is needed to enforce the clause.

Similarly, in a recent Saskatchewan decision, the court stated that a general contractor can only rely on a “paid when paid” clause if the terms of the contract between the contractor and subcontractor clearly state such a condition.

Recent cases dealing with paid when paid clauses in construction contracts have not altered the manner in which provinces will interpret these clauses. That is to say that Ontario and Alberta continue to rely on those decisions which hold that the subcontractor is not entitled to pay until such time as the owner pays the contractor; whereas Nova Scotia, P.E.I., British Columbia and Saskatchewan will only extend the time under which a contractor is obligated to pay. That said however, it seems that all courts regardless of the province, appear to approach the application of a paid when paid clause cautiously, and may even, by default, favour findings which render these type of clauses invalid unless the clause is clear and unambiguous within the document, and the parties are aware of its meaning and possible effect on payments related to the contract.

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