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"PAY WHEN PAID" CLAUSES AND CERTIFIED PAYMENTS REVISITED

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Back in our Summer 2002 Construction Law Newsletter, we wrote about the differing judicial attitudes and approaches across the country towards "pay when paid" clauses. The April, 2003 Ontario decision of Justice Zelinsky in *Harris Steel Ltd. v. Seaboard Surety Co. of Canada* is the most recently reported decision revisiting these clauses, which attempt to shift the risk of non-payment from a general contractor to a subcontractor, and relieve a general contractor of an obligation to finance the costs of performing its work pending payment from the owner.

Harris Steel also looks at the familiar situation where a subcontractor receives instructions to perform extra work, but then no signed Change Order is issued, setting up the dispute whether there is a contractual obligation to pay for that work.

The Ontario Superior Court of Justice considered whether the subcontractor, Harris Steel, was entitled to be paid both for extra work not expressly certified by the Consultant/ payment certifier, and for the balance owing on its subcontract for which the general contractor, Marathon Delco Inc., had not been paid by the owner. The answers to both questions would impact on Seaboard Surety, who had issued a Labour & Material Payment Bond on behalf of Marathon.

On the "pay when paid" issue, the question was whether the clause was effective in law. The trial judge held that in order for a general contractor (or surety on an L&M Payment Bond) to avoid payment to its subcontractor when it has not received payment for that work, the "pay when paid" clause must be very clear. It must not be buried in the fine print, but rather drafted to make it abundantly clear to the subcontractor that the risk of non-payment is being shifted to it. The trial judge ruled that the clause was not sufficiently clear to shift the risk of non-payment to the subcontractor, and held that accordingly, the general contractor was obliged to pay and that therefore Seaboard was obliged to pay on the L&M Payment Bond.

On the uncertified "extras" issue, the judge found that the rebar work forming the basis for Harris Steel's claim for extras was critical path work that could not, or should not, have been held up by Harris Steel while it waited for a signed Change Order. The trial judge also found that both Marathon and the Consultant were aware of the extra work Harris Steel was performing, and that they in fact encouraged Harris Steel to do the work without a formal Change Order having

been issued. Therefore, the judge ruled, Marathon was obliged to pay for this extra rebar work.

Seaboard Surety's obligation to pay Harris Steel for the extra work pursuant to the L&M Payment Bond followed the finding of Marathon's obligation to pay for this extra work. Mr. Justice Zelinski quoted from an earlier Ontario case called *Kor-Ban*, where the Court distinguished the realities of critical path construction work from more abstract contract law theory, reminding us that in theory, contractors and subcontractors are supposed to wait for a signed Change Order **before** proceeding with the extra work; but that in practice, critical work cannot wait for the contract administration to catch up to, or confirm, critical on site activities. It is noteworthy that the Judge found that in all cases, Harris Steel had proceeded "in good faith" with the extra work, and that it had been able to establish that Marathon and the Consultant were aware that the extra work was proceeding, and that the owner would be the ultimate beneficiary of that work.

Seaboard Surety had also argued that certification by the payment certifier was a "condition precedent" to any entitlement by Marathon, and therefore Harris Steel, to be paid for the work, and, since some of the disputed work had not been certified as payable by the owner, Harris was not entitled to payment.

The judge was able to avoid this conclusion by ruling that the certification requirement was not sufficiently clear to make it a requirement for payment, and that Marathon had not proved that it did everything it could in order to get the disputed work certified, i.e., that since Harris Steel had no control over the certification process and was at the mercy of Marathon in its dealings with the owners, Marathon owed it a duty to at least try to negotiate increased certification. This last point is an expression what may be an emerging duty placed upon general contractors to act in good faith towards their subcontractors in respect of the certification process.

In summary, "pay when paid" clauses clearly make judges uncomfortable since they seek to shift risk of non-payment from the payor to the service provider, who is often smaller and less able to finance its labour and materials for significant lengths of time. General contractors seeking to impose and rely upon "pay when paid" clauses are well advised to have their current clauses reviewed by counsel to ensure that the clause is clear and sufficiently obvious.

As for payment for extra work in circumstances where there is no signed change order, a more equitable attitude will generally prevail where it is clear that the paying party was aware of the work, or instructed that it be done, and there is a benefit bestowed because of the work.

NEW *CRIMINAL CODE* LEGISLATION CREATES EMPLOYER'S LIABILITY FOR WORKPLACE INJURIES AND DEATH

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On March 31, 2004 Bill C-45 was proclaimed into force amending the *Criminal Code*.

The centerpiece of Bill C-45 is the creation of a new legal duty operating in the Canadian workplace:

- Every one who undertakes, or has the authority, to direct how another person does work or performs a task is under a legal duty to take reasonable steps to prevent bodily harm to that person or any other person, arising from that work or task.

The new legislation redefines the word "everyone" to include not only individuals and corporate entities, but also unincorporated associations such as partnerships.

The amendment relies on the existing definition of bodily harm within the *Criminal Code*; namely any hurt or injury to a person that interferes with the health or comfort of the person and that is more than merely transient or trifling in nature.

A breach of the workplace duty constitutes criminal negligence which, in the event the breach causes death or bodily harm, the breaching party can be prosecuted under sections 220 and 221 of the *Criminal Code*.

The new duty requires the employer to take reasonable steps to prevent bodily harm. At a minimum, this reinforces the existing law that employers should take all reasonable care to ensure that their workplaces comply with OHSA legislation governing the employer's operations.

The responsibility for ensuring compliance falls squarely on the shoulders of the one or more senior officers who are responsible for that aspect of the employer's activities in which a risk of non-compliance leading to bodily harm may exist. If the senior officers depart markedly from the standard of care that, in the circumstances, could reasonably be expected of them, then the senior officers and the employer can be liable in the event that shoddy workplace practices cause bodily harm or, worse, death to an employee.

The offences of criminal negligence causing bodily harm and criminal negligence causing death are ones considered to be "indictable" by the *Criminal Code*. In the case of a corporation, this means that if it is successfully prosecuted for either of these offences, there is a potential for unlimited fines. The *Criminal Code* also makes provision for corporate offenders being placed on probation and for the making of restitution orders.

Individual offenders face the possibility of not only fines and probation, but also very lengthy prison sentences: in the case of criminal negligence causing bodily harm, ten years; and, in the case of criminal negligence causing death, life in prison.

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