

CAN I SAFELY RELEASE HOLDBACK IN ONTARIO AFTER MARCH 16, 2020?

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On Friday, March 20, 2020, the Government of Ontario issued Ontario Regulation 73/20 further to the *Emergency Management and Civil Protection Act*, R.S.O. 1990 c. E.9. The Regulation suspended any limitation period under any statute, rule, by-law or order of the Government of Ontario. The suspension of limitation periods is “for the duration of the emergency” and retroactive to March 16, 2020.

Undoubtable this measure is intended to protect the public from the expiry of legal rights in circumstances where the COVID-19 pandemic prevents parties from taking timely steps normally available to them to preserve those rights. However, this measure may have an unintended consequence: namely, it may prevent the release of holdback further to the *Construction Act*, R.S.O. 1990, c. C-30 (the “*Act*”). Quite simply, holdback can be safely released only when the underlying liens have expired. If liens do not expire, holdback cannot be released without the risk of the payor having to pay the same sums twice.

By way of background, every payor to a construction project (an “improvement” under the *Act*) is obliged to retain a 10 per cent holdback on all payments made to payees during the course of the construction of the improvement. The holdback in the hands of the payor is intended as a reserve fund for the benefit of all suppliers of labour and materials below the level of the immediate payee in the construction pyramid. If one such party is unpaid, they have a limited period of time to preserve a claim for lien, which will prevent the further payment of funds, including the release of holdback, until the lien is dealt with, either by discharge (payment) or by vacating the lien (paying security into court). If the lien period has expired and no claims for lien have been preserved, (or previously preserved liens have been discharged or vacated) then the payor can safely release the holdback to its payees, which can, in turn, distribute the holdback to their suppliers.

If a payor releases holdback prematurely, that is, before the liens rights of those who have an interest in the holdback have expired, then the payor risks paying that amount over again. Accordingly, payors take careful steps to ensure they do not release holdback funds until all liens in respect of that holdback have expired pursuant to the *Act*. More particularly, they rely upon sections 25 and 26 of the *Act* to release holdback without jeopardy. Those sections are as follows:

25 Where a subcontract has been certified complete under section 33, each payer upon the contract and any subcontract may, without jeopardy, make payment reducing the holdbacks required by this Part to the extent of the amount of holdback the payer has retained in respect of the completed subcontract, **where all liens in respect of the completed subcontract have expired** or been satisfied, discharged or otherwise provided for under this Act. (emphasis added)

26 Subject to section 27.1, each payer upon the contract or a subcontract shall make payment of the holdback the payer is required to retain by subsection 22 (1) (basic holdback), so as to discharge all claims in respect of that holdback, where all liens that may be claimed against that holdback have expired or been satisfied, discharged or otherwise provided for under this Act. (emphasis added)

In virtually all cases, parties to a construction project rely upon the passage of time to ensure the underlying liens have expired before releasing holdback. Typically, parties wait 60 days (previously 45 days prior to the recent amendments to the *Act*) after the publication of the certificate of substantial performance to know with certainty, that if they search title on day 61 and find no registered liens, the lien period with respect to all underlying liens has expired. They can, with certainty and without jeopardy, release the holdback under section 26.

The expiry of liens is governed by section 31 of the *Act* which provides that liens will expire at the conclusion of the 60-day period next following the earliest of the events listed, which include the publication of the certificate of substantial performance or the day the contract was completed, terminated or abandoned or the last day of supply, in the case of a subcontract. The *Act* has mechanisms allowing payors to know when the lien period has expired and thus, when they can safely release holdback further to sections 25 or 26 set out above.

However, the new Regulation 73/20 provides as follows:

“Any provision of any statute, regulation, rule, by-law or order of the Government of Ontario establishing any limitation period shall be suspended for the duration of the emergency, and the suspension shall be retroactive to Monday, March 16, 2020.”
(emphasis added)

On a plain and ordinary reading of this provision, it is difficult to argue that section 31 of the *Act* does not meet the criteria of “any provision of any statute... establishing any limitation period.”. As a consequence, section 31 of the *Act* is suspended and construction liens no longer expire “for the duration of the emergency.” If they do not expire, then there is no way to rely upon their expiration to safely release holdback further to sections 25 or 26 of the *Act*.

It is true that both sections 25 and 26, as an alternative to the expiry of liens, also allow for the safe release of holdback if the underlying liens have been “satisfied, discharged or otherwise provided for” under the *Act*. This typically refers to circumstances where a party entitled to a lien has already been paid in full, or where a party’s claim for lien has been vacated by the payment of security into court. In the vast majority of cases, parties rely upon the expiry of the lien period for the safe release of holdback. Since liens can no longer expire, payors cannot release holdback without jeopardy and may (understandably) be reluctant to do so. Project financiers, which usually require proof of the expiry of the lien period prior to releasing or advancing the holdback, may (understandably) be unwilling to do so given such uncertainty.

The inability to release holdback and get the holdback funds into the hands of small business and construction workers is certainly not what the Government of Ontario intended, but is, unfortunately, a consequence of this new Regulation, to anyone who is paying attention.

There are two immediate solutions to this problem that come to mind. The first is simply to exempt the *Construction Act* from the provisions of Regulation 73/20. This may be justified on the basis that the cure is worse than the disease. This manner of providing limitation relief to those entitled to liens will have the impact of delaying or preventing the release of holdback. In the absence of the new Regulation and notwithstanding the pandemic, it was still possible to preserve claims for lien by registration and to perfect claims for lien by electronically issuing actions to enforce. Using those mechanisms to preserve and perfect liens by the parties that need to do so is not nearly as onerous as slowing down or stopping the release of holdback to the vast majority of trades that do not need to preserve liens.

In the alternative, if the Government of Ontario still wishes to continue to suspend the limitations under the *Act*, then adjustments must be temporarily made to sections 25 and 26 of the *Act* to allow for the safe release of holdback notwithstanding the fact that liens can no longer expire. A potential solution is to look to the priority provisions of section 78 of the *Act* for guidance. At the risk of over-simplification, this provision allows ordinary payment draws (as opposed to release of holdback) to be released provided no liens have been registered, and no written notice of lien has been received, prior to the release of funds. If that criteria is satisfied, the project financier will have priority in respect of such ordinary draw advances and can safely release same.

Thus, sections 25 and 26 should be temporarily amended to allow a payor to safely release holdback (after the 60-day period) provided a title search reveals no preserved liens and that the payor has not received a written notice of lien prior to the release of holdback. The payor satisfying these criteria would not be in jeopardy of paying the holdback twice. It is true that a lien preserved *after* such release of holdback would likely be valueless as a lien. But in circumstances where a lien claimant was otherwise “late” in preserving the lien (because of the pandemic) but managed to preserve the lien before the release of holdback, the claimant would still benefit from the new Regulation.

To be clear, the two solutions set out above are not in force. They are suggested here to solve the problem identified. As it stands, payors cannot safely release holdback for the reasons explained.