## RECENT DEVELOPMENTS OF IMPORTANCE

**Duncan W. Glaholt**
**Markus Rotterdam**
**Glaholt LLP**

### "Made in Ontario" Statutory Adjudication

Exactly ten years ago, we proposed a change in Canada's construction credit scheme to implement interim binding "real time" dispute resolution from "first shovel" to final turnover.[1] In other words: statutory "adjudication". Our informal survey of jurisdictions worldwide revealed that the implementation of statutory adjudication was typically followed by more reliable cash flow and fewer litigated or arbitrated disputes. We argued for uniform legislation in all provinces implementing this scheme.

Fast forward a decade and on 26 September, 2016, the Ontario Ministry of the Attorney General and the Ministry of Economic Development, Employment and Infrastructure published an expert Review by two preeminent Toronto construction lawyers, Bruce Reynolds and Sharon Vogel, recommending wholesale reform of construction credit legislation in Ontario, including the adoption of statutory adjudication. Read from beginning to end, this Review is a major intellectual achievement on its own, but among the 100 recommendations made in the Review, we find the following pertinent to statutory adjudication (summarized):[2]

- Adjudication should be implemented.
- A statutory default scheme should be implied into any contract that does not include the statutory minimum standards.
- Any party to a construction contract or subcontract should be given the right to adjudicate disputes.
- Back-to-back adjudications should be permitted.
- Multi-issue adjudication should be permitted only through consensual contractual.
- The Ministries should select a first tranche of qualified individuals based in key centers such to act as the group of initial adjudicators.
- An Ontario adjudicator should: be a natural person; not be a party to the disputed construction contract and have no legal conflict of interest (or disclose any conflict of interest and obtain the express prior consent of the participating parties); be a member in good standing of a self-governing professional body, such as engineer, architect, accountant, lawyer, or quantity surveyor; have at least seven years of relevant working experience serving the Ontario construction industry; have successfully completed a standardized Ontario training course and thereafter have received a certificate of authorization to adjudicate from the relevant body governing the Act (*i.e.*, the Ministry or prescribed authorized nominating authority), renewable periodically upon proof of continuing education and a clear record; and not be otherwise disqualified (*i.e.*, by reason of bankruptcy, criminal conviction or for any other prescribed unsuitability).
- An adjudicator should be nominated after a dispute has arisen, not at the outset of a Project.
- An adjudicator should be named in the Notice of Adjudication by the party delivering the notice.
- The parties should have two (2) Business Days after delivery of the Notice of Adjudication to agree on an adjudicator, failing which either party would request that the Adjudicator Nominating Authority appoint an adjudicator within five Business Days (p 235).
- A single official Authorized Nominating Authority should administer all adjudications.
- Adjudicators should have immunity from liability.
- A dispute subject to adjudication must flows from a proper invoice under a construction contract or subcontract.
- Disputes valued at under $25,000 can be referred to adjudication or to the small claims court.
- Parties should be free to agree on the fees of the adjudicator and if they cannot agree, the ANA should determine the fees of the adjudicator.
- Each party should bear its own legal costs, which principle can be departed from in cases of bad faith or misconduct.
- The decision of an adjudicator should be binding on the parties and they should comply with the decision until either: a) the dispute is finally determined by legal proceedings or arbitration; or b) by agreement by the parties that the decision of the adjudicator is finally binding.
- Adjudication decisions should be enforced by way of application to the Superior Court of Justice, similar to arbitration awards.
- Parties should maintain their lien rights such that, if a party wants to have a dispute finally determined through a lien proceeding, they can proceed to preserve and perfect a lien and proceed with a lien action.

With these recommendations, we have a scheme worthy of adoption by all provinces, to create a uniform construction credit environment across the nation. If implemented, statutory adjudication in Ontario will strengthen lien and trust legislation, and will co-exist with a robust private surety bond industry.

The original idea behind "real time", interim binding dispute resolution comes to us originally from the private sector in the UK, in response to out-of-control construction industry litigation costs and delays. By 1996 construction industry litigation costs and cash flow delays were crushing the UK construction industry and creating a perceptible drag on the economy. This led to a full scale enquiry and report by a committee chaired by Lord Latham who issued two reports in 1993 and 1994, entitled *Trust and Money and Constructing the Team* respectively. As a result of these reports, the UK government passed sections 104 to 117 of the *Housing Grants, Construction and Regeneration Act 1996*, governing construction contracts and, in s. 108, imposing a set of minimum standards for statutory adjudication in

Britain. There were a lot of naysayers at first, notably within the legal profession, but they were all proven wrong. The success of adjudication was undeniable. By 2003 there had been between 9,000 and 12,000 notices of adjudication filed but only 172 judgments in proceedings connected with adjudication. This meant that less than 2% of adjudicated outcomes ended up in litigation. A full scale reappraisal of statutory adjudication occurred in the UK in 2009. The following findings and recommendations were made, reinforcing and broadening the applicability of the statutory adjudication scheme:

- The application of the UK Act was extended to all qualifying construction contracts whether or not they are "in writing";
- The prohibition of "pay when paid" provisions was extended to "pay-when-certified" provisions being used to circumvent the prohibition on pay-when-paid provisions and elongate periods for payment;
- Stricter rules governing the "payment notices"; and
- Defaulting payers were made "liable to pay to the party exercising the right a reasonable amount in respect of costs and expenses reasonably incurred".

This set of reforms served as a starting point for the work of Reynolds and Vogel on the Review here in Ontario. The Review identified eight fundamental components in the current UK scheme:[3]

1. The right to refer a dispute at "any time": A party to a construction contract does not need to wait until the project is finished in order to have a dispute determined by an adjudicator.
2. Notice requirements: A party to a construction contract must have the right to give a notice at any time of his intention to refer a particular dispute to the adjudicator.
3. Seven days to brief an adjudicator: A method of securing the appointment of an adjudicator and furnishing him with details of the dispute within seven days of the notice is mandatory.
4. Twenty eight days to an adjudicator's decision: The adjudicator is then required to reach a decision within 28 days of this referral. It will not be possible to agree in advance of any dispute that additional time may be taken for the adjudication. There are only two exceptions to this rule. First the adjudicator may extend the period of 28 days by a further 14 days if the party refereeing the dispute consents. Second, a longer period can be agreed by consent of all the parties. Such agreement can only be reached after the dispute has been referred.
5. Elementary due process: The adjudicator is required to act impartially.
6. Inquisitorial jurisdiction of the adjudicator: The [*U.K. Construction Act*] requires that the adjudicator "takes the initiative in ascertaining facts and the law." This gives the adjudicator power to investigate the issue in whatever manner he or she deems appropriate in light of the short time scale available.
7. Interim binding decisions, enforceable in court if necessary: The decision of the adjudicator is binding until the dispute is finally determined by legal proceedings, by arbitration or by agreement [...] The [*U.K. Construction Act*] does, however, go on to say that the parties may agree to accept the decision of the adjudicator as finally determining the dispute.
8. Adjudicator immunity: The adjudicator cannot be held liable for anything done or omitted in the discharge of his function as an adjudicator unless acting in bad faith. This protection is extended to any employee or agent of the adjudicator.

If Ontario passes legislation on this tried and true model, "Made in Ontario" adjudication will occur in "real time", as the project progresses, and not as a wasteful quasi-forensic exercise at or long after substantial completion when small disputes have grown to unmanageable proportions.

For example, a dispute as to whether work is compensable extra work or not, or as to whether deductions or set offs from a progress billing, for example, will result in an immediate Notice of Adjudication and 40 days later, after a reasonable but highly summary process, a determination which remains binding and enforceable until the conclusion of the project. If money is due, money will change hands and cash flow will be restored when it matters most: during construction. If money is not due, performance will proceed and there will be no opportunity for a contractor to withhold performance to improve bargaining position. In short, it will be very hard indeed to "game" the system.

The closest analogue to "made in Ontario statutory adjudication" is likely the well-known "Dispute Review Board", in any of its various forms. Unlike adjudicators, however, Dispute Review Boards are typically standing boards, empaneled throughout the entire project. Also unlike adjudicators, Dispute Review Boards are often empowered to issue only advisory "Recommendations" and not interim binding rulings.

As envisioned by the Review, "Made in Ontario" statutory adjudication will likely include a minimum set of procedural standards written by statute into every construction contract in Ontario by statute, like the present s. 5 of the Ontario *Construction Lien Act* which amends every contract or subcontract in so far as is necessary to be in conformity with the Act.

Reynolds and Vogel suggest that adjudicators should be natural persons, not involved in any way with the parties to the dispute, free of conflict of interest (at least, free of conflict of interest that has not been expressly waived by the parties) and that they be members in good standing of a self-governing professional body, such as engineers, architects, accountants, lawyers, or quantity surveyors with at least seven years of relevant working experience serving the Ontario construction industry. Reynolds and Vogel propose a certification scheme to support basic standards and continuing education.

Finally, what disputes will get adjudicated and how? Based on the experience of other jurisdictions, disputes referred to adjudication will include the following: any dispute that flows from a proper invoice under a construction contract; valuation of work, services, materials and equipment supplied to an improvement and claimed as part of a proper invoice; other monetary claims made in accordance with the provisions of the construction contract that have been claimed in a proper invoice, including the change orders and proposed change orders; claims in relation to any security held by a party under the construction contract; set-offs and deductions against amounts due under a proper invoice as set out in the notice of intention to withhold or otherwise; and delay issues insofar as they relate to claims for payment.

Importantly, "Made in Ontario" adjudication will permit "back-to-back" adjudications, allowing the contractor, subcontractor, and even suppliers to participate in a process that will resolve all issues, deep into the construction pyramid, in real time. If our "Made in Ontario" process resembles that of other jurisdictions, the adjudication process will be commenced with a notice of adjudication, likely a prescribed form requiring the party serving notice to set out the nature of the dispute, the redress sought and propose an adjudicator. The parties would then have a very short period (two business days perhaps) to agree on an adjudicator, failing which one would be appointed for them off by a provincially sanctioned appointing authority from a roster of qualified adjudicators. Within another very short period of the adjudicator's appointment (five calendar days perhaps), the referring party would send a referral notice to the adjudicator (and every other party), including the notice of adjudication, the underlying contract and invoice (with backup) and any documents the party intends to rely upon in the adjudication.

The Review proposes leaving the design of the process thereafter to the adjudicator. Importantly, it is also recommended that the adjudicator occupy an "inquisitorial" role, like a magistrate in civil law jurisdictions. This will allow the adjudicator to become an active agent in the inquiry, and to get to the bottom of the matter. The adjudicator who will consult with the parties and direct how evidence is taken, if, when and how experts should testify, what written or oral submissions are required from the parties, whether or not a site visit is necessary, *etc.*

No matter what the process is adopted by the adjudicator, the adjudicator will be obliged to wrap it all up and render a reasoned written decision within another very short period, coinciding with a reasonable payment cycle (30 calendar days perhaps) from the date of the referral notice. This reasoned written decision becomes binding on all parties until the dispute is either finally determined by legal proceedings (including lien proceedings), or by arbitration (if provided for under the contract, or the parties agree to arbitrate). Alternatively, the parties may simply agree that the decision of the adjudicator is finally binding. Experience in other jurisdictions strongly indicates that it is a very rare case indeed in which parties will choose to litigate or arbitrate an adjudicator's determination at the end of a project.

Adjudicator's interim binding decisions are enforceable by courts. In Ontario, the adjudicator's decision could be enforced by way of summary application to the Superior Court of Justice, in a manner similar to that employed in respect of the awards in domestic arbitrations under the *Arbitration Act, 1991*.

The "Made in Ontario" adjudication regime proposed in the Review will go hand in hand with a proposed prompt payment regime. The Review recommends the implementation of this statutory prompt payment scheme at all levels of the construction pyramid, allowing contractors to notify subcontractors of nonpayment by owners, and to undertake to commence or continue proceedings necessary to enforce payment as a means of deferring their own payment obligations. Upon delivery of a proper invoice followed by certification for payment the Review recommends that unless agreed otherwise, owners must pay general contractors within 28 days following the submission of a proper invoice, and that general contractors pay their subcontractors within a further seven days from receipt of payment from the owner. Such payment would remain subject to an owner's right to deliver a "notice of intention to withhold payment" within seven days following receipt of the invoice. That notice would have to set out the amount withheld the reason for withholding it. This notice, if disputed, would likely trigger an adjudication.

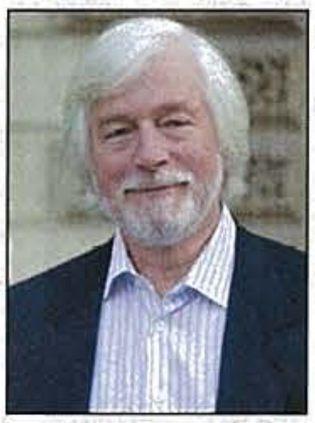
What could go wrong? It is noteworthy that most jurisdictions which have enacted an adjudication model do not have a construction lien regime like Ontario's. The Review recommends maintaining the *Construction Lien Act* in addition to the new adjudication legislation, which makes a great deal of sense. The hope would be that once the industry settles in to the idea of statutory adjudication, the number of unresolved disputes over payment, requiring resort to lien and trust remedies, will drop markedly. The Review recommends that parties maintain their lien rights such that, if a party wants to have a dispute finally determined through a lien proceeding, they can proceed to preserve and perfect a lien and proceed with a lien action.

Similarly, if disputes are resolved quickly in "real time" by adjudication, the unworkable relationship between provincial lien and trust legislation and the federal *Companies' Creditors Arrangement Act* and *Bankruptcy and Insolvency Act* will be improved insofar as there will be very little uncompensated value for the federal statutes to expropriate for the benefit of general creditors.

The time is right for all provinces to get behind the Ontario reforms and render uniform across the country that which is now an unnecessarily complex

patchwork of rights and remedies, themselves historical artifacts of earlier, less sophisticated construction industry economies. Less working capital should be diverted into unproductive dispute resolution across the country, and Ontario's "Made in Ontario" adjudication scheme is a solid step in that direction. The model is tried and tested internationally. It works. It accomplishes its goals. It is to be hoped that the Reviews' recommendations on adjudication and prompt payment will be adopted by our Legislature as a priority. ■

1. Duncan W. Glaholt, The Adjudication Option: The Case for Uniform Payment & Performance Legislation in Canada (1996), 53 C.L.R. (3d) 8.
2. Bruce Reynolds, Sharon Vogel, *Striking the Balance: Expert Review of Ontario's Construction Lien Act*, April 30, 2016.
3. Reynolds & Vogel, supra, note 2, citing Nicholas Gould & Charlene Linneman, "Ten Years on: Review of Adjudication in the United Kingdom" (2008) 134:3 *J Professional Issues in Engineering Education and Practice.*



**Duncan W. Glaholt,** *Glaholt LLP*
Tel: (416) 368-8280 • Fax: (416) 368-3467 • E-mail: dwg@glaholt.com

Duncan W. Glaholt, CArb, is the Founder and partner of the internationally recognized construction law firm of Glaholt LLP. This firm is consistently rated one of Canada's most highly recommended mid-sized construction law practices. Mr. Glaholt is an experienced arbitrator and mediator. Mr. Glaholt has acted as court-appointed monitor and is Certified as a Specialist in Construction Law. Mr. Glaholt is the recipient of the 2014 OBA Award of Excellence in construction law. Mr. Glaholt is the author of the annual *Conduct of a Lien Action*; *Conduct of a Trust Action*; co-author of the annual *Annotated Construction Lien Act*; *Construction Builders' and Mechanics' Liens in Canada*; *Halsbury's Laws of Canada, Construction* and *Halsbury's Laws of Canada, Alternative Dispute Resolution* and *The Law of ADR in Canada: An Introductory Guide*. Adjunct Professor, Faculty of Law, University of Toronto, a Governor, Founding Fellow and past president of the Canadian College of Construction Lawyers, Fellow of the American College of Construction Lawyers, Founding Fellow of the International Academy of Construction Lawyers and past editor of the *Journal of the Canadian College of Construction Lawyers*. He is past Chair of the William Osler Health System, Ontario's first 3P public hospital.

**Markus Rotterdam,** *Glaholt LLP*
Tel: (416) 368-8280 • Fax: (416) 368-3467 • E-mail: mr@glaholt.com

Markus Rotterdam is Director of Research at Glaholt LLP in Toronto. In that capacity, he is responsible for developing legal arguments and solutions when the firm's lawyers are presented with complicated, critical legal issues. He is also responsible for all research for the firm's various publications. Markus has co-authored several books on construction law and alternative dispute resolution with Duncan Glaholt and has published numerous articles and presentations on those topics. He has provided the primary research and front-line editing for Duncan's other books: *Construction, Builders' and Mechanics' Liens in Canada*, 7th edition (Carswell, 2005), *Conduct of a Lien Action* (Carswell), *Annotated Ontario Construction Lien Act* (Carswell) and *Conduct of a Trust Action* (Carswell). Markus is the editor of the *Construction Law Letter*, a bi-monthly national newsletter to the construction industry published by LexisNexis. After graduating from law school at Ruhr-Universität Bochum with a Dipl-Jur, he obtained a Master of Laws at Osgoode Hall Law School in Toronto. He also holds an Academy Certificate from the Hague Academy of International Law, The Netherlands.