

CONSTRUCTION LAW LETTER



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GUEST ARTICLE



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TERMINATION: TREAT CONVENIENCE WITH CAUTION

What does “termination for convenience” mean? Many construction contracts contain termination for convenience clauses, which purport to allow a party (typically an owner) to terminate an agreement without cause. Such clauses may go further and state that the right to terminate can be invoked in the owner’s sole and unfettered discretion, without requiring any wrongful act or inaction by the other party. Despite wording providing for unilateral discretion, are these rights to terminate for convenience limited by law?

The use of termination for convenience clauses first became common in projects involving government agencies or other publicly funded owners. That continues to be the case, and now their use is becoming more common on public and private projects internationally. Despite the growing prevalence of such clauses, the current state of the law in Canada as to the circumstances under which termination for convenience can be properly invoked remains unclear.

It is difficult to reconcile a broadly worded termination for convenience clause with the organizing principle of good faith applicable to Canadian contracts following the Supreme Court of Canada’s decision in *Bhasin v. Hrynew*. As outlined in *Bhasin*, the organizing principle of good faith “is simply that parties generally must perform their contractual duties honestly and reasonably and not capriciously or arbitrarily”. Good faith requires that a contracting party “should have appropriate regard to the legitimate contractual interests of the contracting partner”.

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How can one party's unilateral decision to terminate without cause have "appropriate regard" for the other party's interest in continuing the contract? Appropriate regard will be determined on a case-by-case basis, and will depend upon the precise wording of the termination for convenience clause and the circumstances giving rise to the termination.

One example of a termination for convenience clause can be found in the new 2016 version of the Canadian Construction Documents Committee standard form Cost Plus Contract (CCDC 3). GC 7.1.7, which was not included in the previous 2008 version of CCDC 3, now states that:

7.1.7 The Owner may, if conditions arise which make it necessary for reasons other than as provided in paragraphs 7.1.1 [termination on account of bankruptcy] and 7.1.4 [termination for uncorrected default], terminate this Contract by giving Notice in Writing to that effect to the Contractor.

GC 7.1.9 goes on to provide that if an Owner terminates the contract under 7.1.7, it must reimburse the Contractor for all work performed and its fee up to the effective termination date, along with reasonable termination or suspension costs and a reasonable amount for anticipated loss of profit. While included in the CCDC 3 language, the last requirement to provide compensation for anticipated loss of profit is not always included in a termination clause. Where it is not included, and a contractor would *prima facie* not be entitled to such compensation, they may be incentivized to sue for wrongful termination of the contract, in bad faith or otherwise.

The language of a termination for convenience clause is critical to how a court will assess termination under it. Courts seek to give effect to an agreement as the parties intended it to operate. In the above CCDC 3 example, a court might assess whether termination was actually "necessary" for the owner, as opposed to merely convenient or desirable. With some exceptions, courts are generally reluctant to find an implied right to terminate a contract. Courts will likely be similarly reluctant to expand the scope of a right to termination beyond the circumstances as described in the language of an agreement.

Even in cases where termination for convenience clauses provide unfettered discretion, owners may not wish to take advantage of them where they expose an owner to greater liability for the contractor's costs. In the recent commercial contract case of *Bombardier Transportation Canada Inc. v. Metrolinx*, Metrolinx attempted to terminate its contract

with Bombardier for material default and Bombardier successfully obtained an injunction to prohibit the termination until the contractual dispute resolution process could take place. Justice Hainey noted that Metrolinx could have instead taken advantage of its termination for convenience clause under GC 13 of the contract:

[11] (d) Under this provision, MTX may, by written notice to BTC, terminate the Contract for its own convenience any time, if MTX considers such action necessary or in the best interests of MTX. MTX's right to terminate the Contract for convenience is an absolute and unconditional right and is not subject to the dispute resolution process under the Contract. In the event of a termination for convenience, BTC is entitled to payment of certain specifically listed amounts, described as the Termination Costs.

Metrolinx could have terminated the contract for convenience, but apparently wanted to avoid having to pay Bombardier's termination costs. If Metrolinx had taken this route, its decision to terminate for convenience would have been final and not subject to dispute resolution under the contract. However, Metrolinx chose to pursue termination for material default, exchanging the termination costs for the risk that Bombardier could enforce the dispute resolution process with respect to the engineer's determination that there was material default. Bombardier won its challenge and an injunction now prevents (or at least postpones) termination of Bombardier by Metrolinx for material default until the dispute resolution process occurs.

While invocation of a termination for convenience clause may be unrestricted in a contract, an owner could have its own internal restrictions. Public Works and Government Services Canada has established a policy to guide Government of Canada organizations in invoking termination for convenience clauses in contracts for the procurement of goods, services and construction. Section 8.135.5.b of the Supply Manual provides that termination for convenience applies when a termination for default cannot be considered because the contractor is not in default; and a ter-

mination by mutual consent would not be more advantageous to Canada.

The Termination for Convenience Process set out in Annex 8.3 to the Supply Manual provides for involvement of the Policy, Risk, Integrity and Strategic Management Sector (PRISMS) termination claims officer, following issuance of a notice of termination. The termination claims officer's responsibilities include, among other things:

- assessing the contractor's request for any upward adjustment of the contract price;
- determining, defining and arranging audits, as required; and
- negotiating a final settlement with the contractor.

It is unlikely that these specific requirements will be referenced in a contract and they may not be enforceable by a contractor who is facing termination for convenience by a Government of Canada organization. However, the policies could be taken into consideration by a court in the context of an allegation of bad faith. A Government of Canada organization's ability to demonstrate compliance with the Supply Manual would seemingly be integral to it arguing that any such termination for convenience was conducted in good faith. The same could be true of other owner organizations with respect to their own policies and procedures that a contractor might have had knowledge of and reasonably relied upon.

All this does not provide a simple answer to the question of whether and under what circumstances, (since the decision in *Bhasin*) termination of a construction contract for convenience can be invoked in good faith. There is not yet a decided case that is directly on point. In anticipating what a court might determine in such a situation, it is potentially helpful to refer to cases involving termination of other types of commercial contracts. Much of the post-*Bhasin* termination-related case law concerns ongoing employment contracts lacking a finite scope of work or time period. It is difficult but possible to identify cases which are more analogous to construction projects.

In the 2016 case of *Atos IT Solutions and Services GMBH v. Sapient Canada Inc.*, Siemens was a sub-

contractor for Sapiient on a software system replacement project. The evidence showed that Sapiient was seeking to terminate Siemens' subcontract to improve its own financial position on the project. The dispute resolution section in the subcontract required the parties in good faith to attempt to resolve any dispute, first informally involving executives. Siemens sought to engage the dispute resolution process, but Sapiient did not respond and three days later it terminated the subcontract. In so doing, Sapiient was found to have terminated the subcontract in bad faith, and was liable for Siemens' damages associated with the wrongful termination. Siemens' damages included an amount in respect of the estimated loss of profit it suffered as a result of early termination of the subcontract.

It is important to note that in this case Sapiient initially purported to be terminating Siemens' subcontract for material breach under section 17.2 of the subcontract. Later at trial, Sapiient attempted to advance the argument that, in the alternative, if there was no material breach, its letter also had the effect of providing notice of termination for convenience under section 17.4, applicable to one part of the work under the subcontract. Justice Pattillo did not accept this argument, finding that Sapiient primarily intended to terminate and take over the other portion of the work, not subject to termination for convenience, and therefore did not intend to rely on section 17.4.

The *Atos* situation is analogous to one which might occur on a construction project. An owner or contractor who finds itself in Sapiient's position, seeking to improve its own financial position, should be very careful about how it exercises a right to terminate, for convenience or otherwise. Sapiient knew the project was no longer economically advantageous, and a recent meeting with the owner, Enbridge, regarding increased costs did not go well. In the months leading up to termination Sapiient ceased cooperating with Siemens, in a manner which would later be found by Justice Pattillo to be in bad faith.

A party may follow their obligations as set out in a contract, but if they do so uncooperatively or capriciously, that may be justification for a find-

ing of bad faith. As outlined in *Bhasin*, "appropriate regard" for the legitimate interests of the other party will vary on a case-by-case basis. A party who considers termination for convenience should evaluate whether its own conduct meets an appropriate standard for good faith before proceeding. Similarly, a contractor who has been terminated for convenience should consider whether the party invoking termination has acted in good faith leading up to and including invocation of the termination.

The resulting difference to the economic position a terminated party on a construction project may find themselves in as a result of termination for convenience versus termination for cause may be very significant, justifying a challenge on the basis of bad faith. Hopefully, such a challenge will eventually lead to a determinative court decision in Canada, allowing future owners, contractors and subcontractors to know how termination for convenience may not be as "convenient" as stated in the words of a contract.

CASE SUMMARY



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EXAMINING THE STATUTORY RIGHT OF SET-OFF

Architectural Millwork & Door Installations Inc. v. Provincial Store Fixtures Ltd.

1587855 Ontario Inc. v. Contract Glaziers Corp.

Most readers are likely aware that the majority of construction lien legislation across Canada imposes trust obligations on owners, contractors and subcontractors for the benefit of those contracted to them on a project (among other potential beneficiaries). This is intended to encourage prompt payment and to provide another layer of protection for those adding value to a project.

However, trust obligations are not always absolute. For example, s. 12 of Ontario's *Construction Lien*