

Presented at the CESF Client Seminar
November 24, 2011

Practical Solutions for Managing Risk

Presenters: Sharon Vogel
Karen Kiang
Denise Bambrough



What Current Issues are Relevant to the Management of Risk?

1. Project Security
2. Know Who You Are Contracting With
3. Avoiding Liability for Breach of Trust



Project Security

Sharon Vogel



What Kinds of Performance Security are Available in the Market Today?

Default Security

1. Surety Bonds
 - CCDC standard form performance bond wording:
"Whenever the Principal shall be, and declared by the Obligor to be, in default under the Contract, the Obligor having performed the Obligor's obligations thereunder, the Surety shall promptly..."
(CCDC 221-2002 wording)
2. Subcontractor Default Insurance
3. Parental Guarantees



What Kinds of Performance Security are Available in the Market Today?

Demand Security

1. Letter of Credit
 - Letter of Credit wording:
"We hereby authorize the Beneficiary to draw on [the Bank] in respect of this Letter of Credit at any time upon written demand for payment made upon us accompanied by a dated and signed certificate..."
2. Reserve Accounts
3. Holdbacks – CLA Holdbacks and Contractual Retainage
4. Bank Guarantees
5. Demand Bonds



What Kind of Security is Appropriate for any Given Project?

1. Default or Demand Security?
2. Quantum?



Custom Bond Wordings – Moving Beyond “Sticks and Bricks” Coverage

Examples:

- Indemnity Wording:

“and shall indemnify and keep indemnified the Oblige and the officers, servants and agents thereof from all, and all manner of damage, loss, expenses, claims and demands arising out of any breach of the said Contract, or any of the covenants or conditions therein contained...”



Custom Bond Wordings – Moving Beyond “Sticks and Bricks” Coverage

Examples:

2. AIA A312-2010:

- “.1 the responsibilities of the Contractor for correction of defective work and completion of the Construction Contract;
- .2 additional legal, design professional and delay costs resulting from the Contractor’s Default, and resulting from the actions or failure to act of the Surety under Section 5; and
- .3 liquidated damages, or if no liquidated damages are specified in the Construction Contract, actual damages by delayed performance or non-performance of the Contractor.”



Know Who You Are Contracting With

Karen W. Kiang



Due Diligence

• Defining the relationship:

- Owner – Contractor
- Contractor – Subcontractor
- Lenders
- Surety and Insurance

• Researching companies and their principals:

- Industry presence – good, bad
- Internet – Google, Facebook, LinkedIn
- Corporate searches
- Credit history searches



What you want to know

• Actual corporate structure

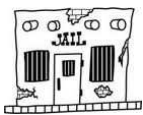
- Directing minds
- Existence of shell companies

• Credit history

• Reputation



What are you trying to avoid?



Jail



Making Less Money



Consequences

- **Corruption of Foreign Public Officials Act**

- Enacted in 1998
- 2005: Hydro-Kleen Group Inc.: \$25,000 fine
- June 2011: Niko Resources: \$9.5 million fine
- Compare to U.S. legislation

- **Blacklisting**

- Private sphere – qualified bidders
- Public sphere – Quebec Bill 35



Avoiding Liability for Breach of Trust

Denise Bambrough



What are Trust Funds?

- All amounts owing to or received by a contractor or subcontractor on account of the contract/subcontract price of an improvement (s. 8(1))
- Beneficiaries of the trust are subcontractors and other persons who have supplied services or materials to the improvement who are owed amounts by the contractor/subcontractor
- The trustee shall not “appropriate or convert” any part of the fund to their own use or to any use inconsistent with the trust, until all subcontractors and other persons who supply to the improvement are paid (s. 8(2))



Proper Payments From Trust Funds

- Every payment by a trustee to a person the trustee is liable to pay for services or materials supplied to the improvement discharges the trustee's obligations and liability to all beneficiaries of the trust to the extent of the payment (s. 10)
- The trustee can also 1) reimburse itself, and 2) discharge a loan, to the extent that it used non-trust funds/the lender's money to pay for the supply of services and materials to the improvement (s.11)



Who Else May Be Liable for Breach of Trust?

Every director or officer of a corporation and any person, including an employee or agent of the corporation, who has effective control of a corporation or its relevant activities, who assents to, or acquiesces in, conduct that he or she knows or reasonably ought to know amounts to a breach of trust by the corporation (s. 13(1))



Accounting For Trust Funds

- The onus is on the trustee to demonstrate proper use of trust funds
- It is a breach of trust to pay trust beneficiaries on one project with trust funds from another (*St. Mary's Cement*)
- Commingling trust funds in a general operating account constitutes a breach of trust (*S.E. Rozell & Sons*)
- S. 12 of the *Construction Lien Act* allows the trustee to "retain" from trust funds (but not spend) money it claims it is owed by the beneficiary (*Datasphere Sales*)



Practical Recommendations

- Keep accurate and detailed records of all receipts and expenditures
- Maintain a separate bank account for each project
- Don't pay "overhead" expenses with trust money
- Retain but don't spend money withheld because of a dispute
- Directors, officers and others with effective control must use due diligence



Thank you



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New Project Delivery Models, Green Building and Other Innovations

Presenters: Matthew Alter
Bruce Karn
Dan Boan



Recent Amendments to the Ontario *Construction Lien Act*

Matthew R. Alter

These materials are designed to provide general information only and although prepared by professionals, do not constitute legal or professional advice. If legal or other professional advice is required, legal services should be sought.



Recent Amendments to the Ontario *Construction Lien Act*

- Ontario's *Open for Business Act, 2010* (OFBA) amended numerous statutes, including the *Construction Lien Act* (CLA)
- The OFBA amendments to the CLA are the most significant changes to the Province's lien legislation in several years.



Recent Amendments to the Ontario *Construction Lien Act*

Amendments to the CLA consist of the following:

- An expanded definition of "improvement"
- The requirement for condominium developers to publish notice prior to registration
- The elimination of the Affidavit of Verification from Claims for Lien
- The elimination of the requirement for a "sheltering statement" when vacating the registration of Certificates of Action



Recent Amendments to the Ontario Construction Lien Act

The New Definition of Improvement

- S.1(1) - Definition expanded to include:

“the installation of industrial, mechanical, electrical or other equipment on land or on any building, structure or works on the land that is essential to the normal or intended use of the land, building, structure or works.”



Recent Amendments to the Ontario Construction Lien Act

Amendments Affecting Condominiums

- New s. 33.1 of the CLA requires owners of land intended to be registered under the *Condominium Act, 1998* to publish a notice of intended registration at least 5 days, and not more than 15 days, before submitting the condominium description for approval.



Recent Amendments to the Ontario Construction Lien Act

Repeal of the Affidavit of Verification

- S. 34(6) of the CLA, which required lien claims to be verified by an affidavit, has been repealed.
- Lien claims are now filed electronically via Ontario's land registry system which created a conflict between the CLA and the *Land Registration Reform Act*.



Recent Amendments to the Ontario *Construction Lien Act*

Elimination of the Sheltering Statement

- S. 44(9) of the CLA has been amended to allow a lien claimant, whose lien is sheltered under a vacated lien, to enforce its lien as if the order to vacate had not been made.
- This amendment eliminates the need for lawyers to provide “sheltering statements” when vacating the registration of a certificate of action.



Green Building – LEED Certification

Bruce Karn



Green Building

1. LEED Certification
2. What Does “Green” Mean to You?
3. Legal Issues
4. Key Points



LEED Certification

- **Types of Certification**
 - New Construction
 - Core and Shell
 - Commercial Interiors
 - Existing Buildings
- **Point-based System**
 - Site Selection
 - Alternative Transportation
 - Water Use Reduction
 - Optimize Energy Performance
 - Regional Materials
 - Daylight and Views



What Does “Green” Mean to You?

Benefits

- Future Savings
- Marketing/Good Will
- Value of Property

Costs

- Design
- Experts
- Materials



Legal Issues

- **Appeal of Certification**
 - Northland Pines High School
- **Unhappy Tenants**
 - Riverhouse One Rockefeller Park Condominium
- **False Advertising**
 - *Gifford v. U.S. Green Building Council*



Key Points

- Define “green” for your project
- Costs vs. Benefits
- Manage risks



New Project Delivery Models

Dan Boan



Project Delivery Models

1. Traditional Model
2. Design Build
3. Build Finance
4. Design Build Finance
5. Design Build Finance Operate/Maintain
6. Construction Manager at Risk
7. Construction Manager Not at Risk



Building Information Modeling (“BIM”)

- BIM provides a 3D design and virtual look at future buildings and structures.
- Combines information from every aspect of the project to identify potential “clashes” early in the process.
- Teams may utilize BIM to analyze the project, including the design, creating “take-offs” and schedules, sourcing materials, etc.
- BIM model can be linked to the construction schedule to decrease project timelines, and optimize workflow.



Integrated Project Delivery (“IPD”)

- Transparent exchange of information between designers and builders.
- Attempt to remove traditional barriers.
- Attempt to decrease project costs by eliminating administrative and other processes.



Integrated Project Delivery (“IPD”)

Characteristics

- Multi-party contracts
 - Contract between Owner, Designer and Contractor.
- Shared Risk/Reward Structures
 - Risks/Rewards distributed across players with rewards accruing to the entire “team” and not individual participants.
- Collaborative, Consensus-Building Decision-Making
 - Important decisions made unanimously amongst the parties.
- Outcome-based Compensation
 - Profit based on accomplishing project outcomes rather than hard bid or cost/plus.
- No Lawsuit Provisions
 - Parties agree to limit or eliminate claims to establish “reduced risk” environment.



Integrated Project Delivery (“IPD”)

Builder’s Role

- Builder interjected into the design process.
- Builder provided knowledge of owner’s overall budget.
- All parties work “for the project”.
- Traditional communication roles removed.
- Remove the traditional “propose/dispose” model of reviewing revisions to the project.
- Remove the “adversarial” relationships for the project.



Integrated Project Delivery (“IPD”)

Example – New England IPD Project

- \$10.5 Million renovation of 55,000 sq. ft. vacant building.
- Single agreement between the owner, architect/engineer, and contractor.
- All decisions to be made unanimously.
- Costs charged to project, without profit. Profits connected to outcomes:
 - Completion of project within budget and within schedule.
 - Achieve LEED® Platinum certification for tenant fit-out, and LEED® Gold for building shell and core.
 - Achieve level of design quality ascertained by a 3rd party design inspector.
- All agreed not to file any lawsuits, except “willful negligence”.
- Used BIM tools.
- Project was completed within budget, within 8 months (including design and construction), LEED® Platinum, and superior quality design.




Integrated Project Delivery (“IPD”)

Will it Work Long-Term?

- Occurrence of traditional claims/issues?
- Third parties that are not part of the “deal”?
- Unrealistic Budgets?
- Change in Financing?



Thank you



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Hot Topics

Participants: Don Pierce
Ian Houston
Bruce Reynolds
James MacLellan



Hot Topics

1. P3s – Emerging Issues
2. Project Priority Disputes
3. Construction Document Management and Claims – Tips to Save Time and Money
4. Insolvency and Construction Disputes
5. Insurer's Duty to Defend and the Own Work Exclusion – Progressive Homes
6. Mediation: By Contract or Court
7. The BPS Directive 2011 – New Mandatory Requirements
8. New CCDC Documents
9. Surety Issues



P3s – Emerging Issues

Donald Pierce, Q.C.



Future Projects

- Municipal Infrastructure Challenge
- Transit
- Hospitals
- IT
- Energy



Financing Issues

- Bank vs. Bond
- Hybrids



Long-term Value of Asset Management in P3's

- Value of lifecycle maintenance
- Value for money evaluation



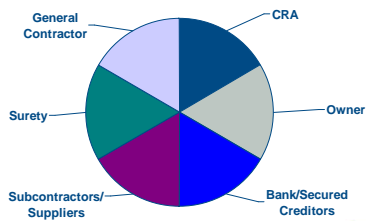
Project Priority Disputes

James MacLellan



Priority Disputes

• Parties with Interest in Contract Funds



General Contractors' Rights

- Payment of subcontractors – “pay when paid”
- Right to set off against subcontract balances for contractual obligations
- Lien Rights
- Trust rights



Bank/Secured Creditor

- Bank holds GSA in first place
- Appointment of Private Receiver/CCAA/Bankruptcy
- Initial Order gives priority for cost of Process
- Observance of provincial lien rights is typically respected
- Protect the funds



Canada Revenue Agency

- Section 224 of Income Tax Act provides “super priority” to CRA for failure to remit withholding taxes
- Serving of Requirement to Pay triggers CRA entitlement
- In past case by case consideration of enforcement of super priority
- Recent trend in CRA to enforce full entitlement
- Owner’s right of set-off



Surety

- Multiple entitlement to project funds
- As performance bond surety
 - Step into shoes of owner and assert owner's rights of set off
- Payment bond surety
 - Step into shoes of lien and trust claimants
- Disputes arise with Owner/Obligee
- Disputes arise with CRA
- Disputes arise with Bank/Secured Creditor



Suppliers and Subcontractors

- Entitlement arises under lien legislation
 - Lien rights
 - Trust rights
- CRA "super priority" trumps entitlement



Construction Document Management: Preparing for claims and litigation

R. Bruce Reynolds



Construction Document Management

- Document management is necessary and important when responding to claims and subsequent litigation
- Having proper document management before claims and litigation arise will save you time and money
 - For every file, have a plan for document retention and document all agreements, correspondence, notices etc. for each project



Proving Claims, Cause and Effect

- Document potential claims
- Open a new cost code for potential claims
- Collect evidence about the potential claim after the issue is brought to your attention and retaining an expert if necessary
- Litigation “hold”



Other considerations in litigation

- Spoliation = intentional or reckless destruction of evidence
 - Better to be careful than to attempt to delete
 - Spoliation leads to adverse inference
 - Can be held in contempt of court
- There is an ongoing obligation to produce relevant documents



Tips for document management

- Educate employees about email risks
- Be aware that personal files and diaries may be produced in litigation
- Consider use of language in correspondence with subtrades and when agreeing to causes and impacts
- Early communication of challenges



Insolvency and Construction Disputes

James MacLellan



The Construction Lien Act v. The Companies' Creditors Arrangement Act

- Construction Lien Act - Ontario
 - Lien must be registered within 45 days and perfected within 90 days of the last day of supply
 - claim must then be set down for trial within 2 years.
- Companies Creditors Arrangement Act (CCAA) - federal
 - typical CCAA order stays all proceedings against the company and prohibits the commencement of new proceedings
 - Lien claimant may lose lien rights unless claimant can have the CCAA order lifted



The Construction Lien Act v. The Companies' Creditors Arrangement Act cont.

- DIP Financing
- *Veltri Metal Products Co., Re (2005) vs. Minneapolis-Honeywell Regulator Co. v. Empire Brass Manufacturing Co. (1955)*



The Construction Lien Act v. The Bankruptcy and Insolvency Act

- Bankruptcy and Insolvency Act (BIA)
- Under the BIA, proceedings are also stayed for all lien claims registered after the proposal
- Lien actions commenced in time can continue but the lien claimant needs to seek leave from the court to obtain judgment against the debtor.



Insurer's Duty to Defend and the Own Work Exclusion – Progressive Homes

James MacLellan



The Problem

- Commercial General Liability (CGL) policies are not performance bonds
- CGLs provide protection from Third Party Claims for damage caused by faulty work
- CGLs include a duty to defend
- CGLs usually have exclusions: the cost of repair faulty work is not covered
- What happens when sued for damages caused by faulty work?



Progressive Homes, Supreme Court of Canada – September, 2010

- Is defective work an accident/occurrence?
 - British Columbia Court of Appeal Answer: No
 - Supreme Court of Canada Answer: Yes
- Why?
 - Property damage caused by faulty work is usually not expected nor intended
 - Property damage is not limited to damage to another's property
 - Property damage can mean damage to the work itself



Was there a duty on Lombard to defend Progressive?

- Yes: possibility of coverage = duty to defend
 - Progressive Homes has already been applied in two recent Ontario cases
 - PCL Constructors v. Encon, October 27, 2010
 - California Kitchens v. AXA, November 5, 2010
- N.B. – the duty to defend ≠ duty to indemnify



Who defends?

- Insurer's obligation v. insured's skepticism (steering the defence)
- Reasonable apprehension of conflict of interest?
 - If yes – independent counsel appointed at insurer's expense
 - If no – insurer appoints counsel and defends at its expense
- Recent examples:
 - PCL v. Encon, October 27, 2010
 - PCL v. Lumberman's, June 25, 2009
- Usually: insurer's counsel defends and reports to insurer and insured



Mediation: By Contract or Court

R. Bruce Reynolds



Mediation: Contractual Mediation

- CCDC2 2008: GC 8.2: Negotiation, Mediation and Arbitration
- CCDC 40: Rules for Mediation and Arbitration of Construction Disputes



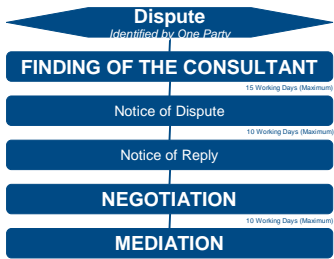
- GC 8.2.1 – Appointment of Project Mediator

- Within 20 working days of contract award:
or
- Within 10 days of Notice in Writing (8.2.1)

- Disputed finding by Consultant can trigger mediation process



GC8.2 Mediation Procedure



- If Mediation fails, on to Arbitration (GC8.2.6)



Mediation Rules: Litigation

MANDATORY MEDIATION

- Ontario – Rule 24.1 of the Rules of Civil Procedure



Ontario Mandatory Mediation

- All actions commenced in Ottawa, Toronto and County of Essex
- Exceptions:
 - Actions on the commercial list in Toronto
 - Actions under the *Construction Lien Act* except trust claims



Innovative Techniques

- Procedural Committee
- Experts Meetings
- Mediation without a mediator



The Broader Public Sector Procurement Directive (BPS)

Ian J. Houston



Who Does the BPS Directive Apply To?

- Includes:
 - Hospitals
 - School Boards
 - Universities
 - Colleges
 - Community Care Access Centres
 - Children's Aid Societies
 - Other organizations receiving \$10M or more in public funding per year (as of January 1, 2012)
- Excludes:
 - Municipalities
 - Local Boards
 - Boards of Health
 - Long-term Care Homes
 - For-profit Organizations
 - First Nations
 - Public bodies under the *Public Service of Ontario Act, 2006*



Background and Structure

- Background
 - Authorized by s. 12 of the *Broader Public Sector Accountability Act (2010)*
 - Replaces the BPS Supply Chain Guidelines issued by the Ministry of Finance in 2009
- Structure
 - **BPS Directive** – 25 Mandatory Policies
 - **BPS Directive Implementation Guidebook** – designed to assist organizations with implementing the Directive
 - **Code of Ethics** – a standard of personal accountability that all BPS Organizations must adopt



Purpose and Principles

- Purpose:
 - Ensure that publicly-funded goods and services (including construction, consulting and IT) are acquired through an open, fair and transparent process;
 - Outline the responsibilities of BPS organizations at each stage of the procurement process; and
 - Ensure that procurement processes are managed consistently throughout the BPS.
- Principles:
 - accountability
 - transparency
 - value for money
 - quality service delivery
 - process standardization



Key Directives

- **1) Segregation of Duties** (3 of requisition, budgeting, commitment, receipt, and payment functions must be separate)
- **3) Competitive Procurement Threshold** (open, competitive process required for any procurement worth more than \$100K; some exceptions apply)
- **6) Posting Competitive Procurement Documents** (required use of accessible electronic tendering system)
- **9) Evaluation Criteria** (transparent evaluation criteria required)
- **10) Evaluation Process Disclosure** (transparent evaluation methodology required)
- **13) Winning Bid** (submissions with the highest score must win)
- **14) Non-Discrimination** (no preferential treatment)
- **16) Establishing the Contract** (must use the contract included in the procurement documents)
- **20) Supply Debriefing** (must disclose all bidders' right to a debriefing following contract award)
- **25) Bid Dispute Resolution** (must provide procedures to fairly handle disputes in a timely fashion)



New CCDC Documents

Ian J. Houston

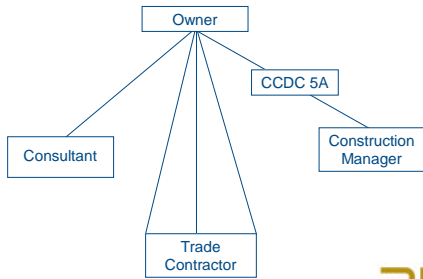


CCDC 5A Construction Management (not at risk)

- Separation of design and construction responsibility
- Construction manager manages construction for owner for a fee, but no privity of contract with trade contractors
- Owner contracts directly with trade contractors and separately with consultant
- CCDC 5A – Construction manager (used to be CCA5)
- CCDC 17 – Trade contractors



Construction Management (not at risk) (cont'd)



Key Features

- Essentially a services contract (advisory services and overseeing Owner/Trade Contractor contracts)
- Basic services expressly described in schedules to agreement (A1, B1)
- No responsibility for design (GC 2.1.3)
- Authority as agent for owner limited to the provision of services (GC 2.1.4)



CCDC 5B Construction Management (at risk)

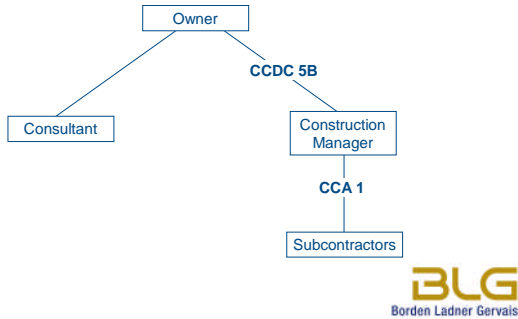
Construction Management Contract for Services and Construction

- Construction Manager at Risk
- Construction Manager as Constructor

Similar pre-construction services as CCDC 5A but very different once construction commences



Construction Management (not at risk) (cont'd)



Key Features

- Privity with Owner and separately with construction trades (subcontractors)
- Responsible for performance of subcontractors
- Expressly not Owner's agent (GC 1.5.2)
- Similar to general contractor (CCDC 2, 3) with pre-construction (CCDC 5A) responsibilities
- List of "Cost of the Work" items similar to CCDC 3 but should be carefully reviewed



Surety Issues

James MacLellan



Surety Issues

- Bonds in the Tender Process
- Payment Bond Identity Crisis
- Surety as Referee



91

Procurement Process

- Surety's role is more prominent
- Bid Bonds, Agreements to Bond and Prequalification Letters
 - - increasing bid frequency
 - - decreasing bid document preparation time
 - - Broker authority
- Compliance litigation



Procurement Process

- Document preparation:
 - Not using stipulated forms
 - Incorrect name of Principal
 - 10% vs. fixed amount
 - Wrong Surety
 - Right Surety wrong seal
 - Bid bond vs. certified cheque
- Role of the Parties in the Process
 - Surety / Broker / Principal



Payment Bond Identity Crisis

- Guarantees that “claimants” will be paid amount due under contract
- Notice required 120 days after Claimant last work on project
- Challenges to the purpose of Payment Bond
 - Uncertain economic times trends
 - Delayed collection
 - Credit insurance
 - negotiation vs. litigation



94

Surety as Referee

- Surety's obligation under Performance Bond is triggered by a default in performance by Principal under the bonded Contract
- Increasing frequency of notices to Surety, not of default but of a “concern” by Obligee
- Raises numerous issues
- Role of Surety in circumstances
- Motive of Obligee in providing notice
- Strength of relationship with Surety is key to success



95

Thank you