

PAYMENT CERTIFICATION AND HOLDBACKS

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Like any other business transaction, a construction contract is ultimately about money. Owners want their projects to come in on time and on budget, and to hold on as long as possible to amounts which secure the completion of the project and the repair of deficiencies, and which protect against legal liabilities. Contractors want to be paid as much as possible as soon as possible. These interests often conflict.

A construction contract of any size will usually involve the Owner making progress payments at regular intervals or on the achievement of performance milestones. Progress payments require the assessment of the amount of work completed – in a stipulated price contract, the percentage completed out of the total scope of the work; in a cost-plus contract, the value of the work to date. On most larger projects, that assessment is carried out by a payment certifying design professional, usually a prime consultant architect, who is identified and recognized as the Consultant by the general contract between the Owner and the Contractor.

Although the Consultant is usually hired by the Owner and acts as the Owner's agent for many purposes, the Consultant is required to act impartially in certifying payment and completion and in otherwise performing the function of the arbiter in the first instance of the requirements of the general contract. This means that the Consultant must interpret and apply the terms of the general contract fairly, rather than for the advantage of the Owner (or the Contractor), in determining payment and holdback amounts and the achievement of substantial completion.

Construction contracts usually set out a detailed process for the project participants to respectively claim, assess, certify and pay progress claims. Generally, the certification of payment is intended to provide a legally enforceable right to payment for the Contractor, once the contractual time period has expired for the payment to be made after certification. However, case authority confirms that this is not an absolute right and can be subject to other provisions set out in the contract or which are implied by the common law, and which entitle the Owner to set

off against certified amounts the value of the Owner's claims of contractual default by the Contractor.

Sometimes a Consultant determines that a payment certificate previously issued needs to be revised, in order to reflect accurately the circumstances prevailing under the contract. If motivated by new information or other reasonable justification, such revision is not only a proper, but a necessary, step for the Consultant to take.

In addition to analyzing the extent of the completed work, the Consultant must also factor into payment certificates any applicable holdbacks. These can include builders lien holdback, deficiency holdback and any additional special holdbacks called for by the contract.

The builders lien holdback is applicable to most construction contracts, unless the project is exempt from the application of the Builders Lien Act. Examples of exempt projects are those involving Federal Crown property or highways. Unless exempt, the retention of holdback by the owner, and in turn down the contractual chain to subcontractors, is mandatory, except that no holdback is to be retained from material suppliers or workers. The 10% statutory lien holdback will be retained from each progress payment, with the intention of its being released 55 days after substantial completion of the contract, assuming that no liens have been filed against the project property. Partial release of the general contract holdback can be made 55 days after certification of substantial completion of a subcontract.

A deficiency holdback is usually determined at the time of the substantial performance inspection by the Consultant, and reflects the estimated cost to carry out the items identified in that inspection as requiring completion or repair. It is the generally accepted custom of the construction trade in British Columbia that a holdback equal to twice that estimated cost will be retained. Many contracts expressly provide for that doubling.

Sometimes contracts provide for additional holdbacks, such as specified amounts or percentages of the contract price to secure the Contractor's performance and completion of the work, including warranty repair work. That type of holdback is intended to augment or replace the security which would more commonly be provided to the Owner by a Performance Bond obtained by the Contractor.

The holdbacks relate to each other as follows. The 10% statutory lien holdback, and any additional amount actually retained by the Owner and not applied to the completion of the contract in the case of default by the Contractor, constitute a fund to satisfy the Owner's liability to subtrade lien claimants. If no Land Title Office liens or legal actions claiming a lien against the holdback are filed, or to the extent that it exceeds their total value, the lien holdback can be released to the Contractor after the expiry of the holdback period. However, the Owner is not absolutely required to release the lien holdback at that time, if the Owner is otherwise entitled under the contract to retain it as another type of holdback; for example, to top up deficiency holdback to reflect the cost to repair additional deficiencies identified after the substantial performance inspection.

The best way for parties to a construction contract to avoid legal disputes arising from payment certification or holdback retention is for them simply to comply with the requirements of the contract and the Builders Lien Act, with a view to achieving timely payment to the Contractor for completed work while affording reasonable protection for the Owner against construction risks.