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Thomas Heintzman specializes in alternative dispute resolution. He has acted in trials, appeals and arbitrations in Ontario, Newfoundland, Manitoba, British Columbia, Nova Scotia and New Brunswick and has made numerous appearances before the Supreme Court of Canada.

Mr. Heintzman practiced with McCarthy Tétrault LLP for over 40 years with an emphasis in commercial disputes relating to securities law and shareholders' rights, government contracts, insurance, broadcasting and telecommunications, construction and environmental law. He was an elected bencher of the Law Society of Canada for 8 years and is an elected Fellow of the American College of Trial Lawyers and of the International Academy of Trial Lawyers.

Thomas Heintzman is the author of *Heintzman & Goldsmith on Canadian Building Contracts*, 5<sup>th</sup> Edition which provides an analysis of the law of contracts as it applies to building contracts in Canada.

## **Is A Pay When Paid Clause Applicable If The Contractor's Account To The Owner Is Reduced For Reasons Unconnected With Subcontractor's Work?**

A pay when paid clause is one of the most contentious clauses in a building contract. Indeed, the clause is outlawed in most circumstances in the United Kingdom and some states of the United States. In Canada, there is conflicting case law about the application and interpretation of the clause. In *Wallwin Electric Services Inc. v. Tasis Contractors Inc.*, the Ontario Superior court recently gave guidance as to when such a clause is applicable, and held that it does not apply if the contractor voluntarily reduces its account to the owner for reasons unconnected to the subcontractor's work.

## Background

A pay when pay clause purports to entitle the contractor to refuse payment to the subcontractor if the contractor has not been paid by the owner. In the *Wallwin* case, the payment clause read as follows:

“(3) Provided that, as a condition precedent, the contractor has been paid the certificate, in which such amount has been included, by the owner.”

The contractor, Tasis said that it had no obligation to pay the subcontractor since it, the contractor, had not been fully paid by the owner. The main contract had been certified to be substantially completed. There were no outstanding deficiencies with respect to the electrical work done by Wallwin and its work was included in the certificates that had been issued by the consultant.

The owner asserted that there were deficiencies in previously certified work. Accordingly, the contractor Tasis subtracted \$150,176.65 from its invoice for these deficiencies. That work was unrelated to the work performed by Wallwin. Tasis was paid for this invoice.

As the judgment in the case recorded, the parties were agreed that

“1. Wallwin made regular applications for payment as provided for in the subcontract.

2. At no time did Tasis or the project consultant make any changes to the amount of Wallwin's applications for payment.

3. At no time did Tasis or the project consultant give notice to Wallwin of any changes to the amount of Wallwin's applications for payment.

4. Tasis was paid by the owner for each certificate in the amount certified.”

Nevertheless the contractor Tasis submitted that “the subcontractors legal entitlement to payment is contingent upon the general contractor being paid, then the subcontractor must bear the risk of nonpayment by the owner to the general contractor; the only exception being where the reason for nonpayment by the owner is the default of the general contractor.”

## Decision of the Ontario Superior Court

The application judge disagreed. He held that the proper interpretation of a “pay when paid clause is as follows:

**“A contractor is obliged to pay a subcontractor when:**

1. the subcontractor makes application for payment,
2. neither the contractor or certifier have given written notice to the subcontractor of a change in the amount the subcontractor has applied to be paid

3. the amount the subcontractor has applied to be paid has been included in a Certificate for Payment, and
4. the contractor has been paid that Certificate for Payment by the owner.”

In particular, the court held that a contractor cannot:

“avoid its obligation to pay a subcontractor by adjusting an invoice to allow for an owner to retain contract funds when a dispute arises over previously certified payments. The certification process creates the obligation to pay. Disagreements over subcontractor applications for payment may be resolved prior to Certificate for Payment being issued, as contemplated at the end of Article 4.2, or they may be resolved after payment, but once the above conditions have been satisfied payment must be made.”

Accordingly, the court held that the subcontractor was entitled to be paid by the contractor.

## **Discussion**

This case is, perhaps, an easy one. It is hard to contemplate that a “pay when paid” clause could be interpreted to apply if the money held back by the owner is not in relation to the work undertaken by the subcontractor and the contractor has been paid in full for that work. The more difficult cases arise when the contractor is unpaid for all or part of the work done by the subcontractor because of, say, the owner’s insolvency or faulty work by the contractor.

The present decision is interesting because it introduces two ingredients into the application of the “pay when paid” clause:

whether there has been a written notice of change in the subcontract and

whether the consultant has certified the payments due under the subcontract.

These ingredients appear to introduce two new hurdles that the subcontractor must get over before payment will be paid. It is unclear where those ingredients come from.

The Canadian law relating to “pay when paid” clauses is complicated by the conflicting decisions of the Ontario Court of Appeal in *Timbro Developments v. Grimsby Diesel Motors Inc.* (where the clause was applied) and the Nova Scotia Court of Appeal in *Arnoldin Construction & Forms Ltd v. Alta Surety Co.* (where the clause was not applied). Until the law is clarified by the Supreme Court of Canada, the proper scope and application of “pay when paid” clauses will be contentious.

**See Heintzman and Goldsmith on Canadian Building Contracts (5th ed.), chapter 6, part 2(d)(i)**

**Wallwin Electric Services Inc. v. Tasis Contractors Inc, 2015 CarswellOnt 3177  
2015 ONSC 1612**

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