

# PAY WHEN PAID CLAUSES POST-PROMPT PAYMENT AND ADJUDICATION

Posted on October 26, 2022

**Categories:** [Insights](#), [Publications](#)

In *Canadian Pressure Testing Technologies Ltd. v EllisDon Industrial Inc.*,<sup>[1]</sup> the Alberta Court of King's Bench recently reinforced the need for contractual clarity and specificity when drafting pay when paid clauses. Anything less may result in the subject clause being found inapplicable or inoperative to limit a party's obligation to make payment.

This bulletin provides a summary of the decision, which does not consider the *Prompt Payment and Construction Lien Act*, RSA 2000, c P-26 (the "**PPCLA**"), given the PPCLA came into force after the underlying project at issue. This bulletin then provides commentary on drafting a pay when paid clause in light of the PPCLA.

## Facts

Canadian Pressure Testing Technologies Ltd. ("**Subcontractor**") applied for summary judgment against EllisDon Industrial Inc. ("**General Contractor**"). The parties had entered into a subcontract for the Subcontractor to provide pressure testing services for piping (the "**Services Agreement**").<sup>[2]</sup>

The Services Agreement included the following clause (the "**Subject Clause**"):

Section 5.3 [General Contractor] shall pay to the [Subcontractor] monthly progress payments net of any applicable Holdback and such payments shall become due and payable no later than five (5) business days after [General Contractor] receives payment pursuant to the terms and conditions of the Prime Contract from the Owner in respect of such Services.<sup>[3]</sup>

Pursuant to the Services Agreement, the Subcontractor completed its work and issued invoices for progress payments, which were paid by the General Contractor. The Subcontractor then issued its final invoices. The General Contractor refused to pay the final invoices on the basis that it had not yet been paid by the owner.

## Analysis

The General Contractor relied on the Subject Clause when refusing to make payment to the Subcontractor for

the final invoices. The General Contractor argued that the Subject Clause ought be interpreted as a “pay when paid” clause, meaning that payment is not due until the General Contractor receives payment from the owner.

The Subcontractor argued that the Subject Clause ought to be interpreted as a “pay no later than” clause. The Subcontractor argued that the clause required payment no later than 5 business days after the General Contractor received payment, but did not otherwise limit the General Contractor’s obligation to pay even where the owner had not made payment.

The Court had to determine whether section 5.3 of the Services Agreement constituted a “pay when paid” clause or a “pay no later than” clause. In its review of Canadian jurisprudence, the Court determined that the Subject Clause lacked certainty. In instances where a subcontractor’s right to payment is diminished, such a clause must be explicit with its intent. In this case, the Court held that the clause was at least ambiguous as it could have been interpreted as a “pay no later than” clause. The Court granted summary judgment in favour of Subcontractor, in turn reiterating the high threshold of certainty a “pay when paid” clause must adhere to.<sup>[4]</sup>

The Court also considered whether the cause of the owner’s failure to pay the general contractor was due to actions of the General Contractor. The General Contractor’s failure to obtain prior approval for the work completed by the Subcontractor contributed to the Court’s decision not to enforce the Subject Clause as a pay when paid clause. In doing so, the Court cited an Ontario decision that held a contractor cannot rely on a pay when paid clause to refuse payment to a subcontractor when the owner’s failure to pay the contractor is a result of an act or default of the contractor.

The takeaways are that:

1. Parties ought to be clear and express when drafting pay when paid clauses.
2. When seeking to rely on a pay when paid clause, the contractor should try to ensure that the reason for the owner’s non-payment is not due to an act or default by the contractor.

### **Applicability of Pay When Paid Under the PPCLA**

Pay when paid clauses will need to be drafted to comply with prompt payment and adjudication legislation in the jurisdictions where such legislation has been introduced.

In Alberta, the statutory prohibition on pay when paid clauses was removed from the PPCLA prior to its enactment. When first introduced into the legislature, Bill 37 included the following section 32.3:

No effect of prohibition on pay

32.3 Any provision of a contract that provides that a contractor or subcontractor will only be obligated to pay a subcontractor with whom they have a contract after they have received payment for work done or

materials furnished is of no force or effect

This prohibition was subsequently removed prior to the enactment of the PPCLA. The PPCLA provides for statutory timelines for payment and the issuance of notices of non-payment or to dispute payment where appropriate. Please find McMillan LLP's bulletin on the PPCLA generally [here](#).

Parties will need to comply with requirements of the PPCLA, including the issuance of the requisite notices where payment is not being made within the statutory timelines. It should be noted that ss. 5 and 32.3(4) of the PPCLA appear to render pay when paid and similar clauses void unless they are expressly drafted to comply with s. 32.3(5) of the PPCLA. Provided that is done, pay when paid clauses may still be utilized. Examples where pay when paid clauses may potentially be used assuming consistency with the relevant provisions of any applicable prompt payment and adjudication legislation include:

- By a contractor to limit the contractor's obligation to pay a subcontractor in the event of the insolvency of an owner.
- By a contractor to rely on a determination made in respect of a dispute between an owner and the contractor to limit payments to a subcontractor.
- By a contractor to rely on a settlement of a dispute between an owner and the contractor to limit payments to a subcontractor.

We anticipate judicial guidance in the future on the enforceability of such clauses and their uses within statutory prompt payment and adjudication regimes.

McMillan's National Construction Group will be closely watching any judicial or other interpretation of the enforceability of "pay when paid" clauses in conjunction with prompt payment and adjudication regimes.

[1] [ps2id id='1' target='']*Canadian Pressure Testing Technologies Ltd v EllisDon Industrial Inc*, 2022 ABKB 649 ("**Canadian Pressure**").

[2] [ps2id id='2' target='']*Ibid* at para 1 - 2.

[3] [ps2id id='3' target='']*Ibid* at para 3.

[4] [ps2id id='4' target='']*Ibid* at paras 12, 21 – 24.

by [Preet Saini](#), [Michael Briggs FCIArb](#), [Jamieson Virgin](#)

### **A Cautionary Note**

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

© McMillan LLP 2022

The logo for mcmillan, featuring the word in a lowercase, sans-serif font. The 'm' and 'c' are in a dark red color, while the 'm', 'i', 'l', 'l', 'a', and 'n' are in a light blue color. The logo is positioned in the upper left corner of the page.

mcmillan