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JUSTICE MATTERS

Civil Litigation

This newsletter is intended to provide insight for our clients on relevant litigation issues.

Securing Judgments in Cases Involving Real Property: Certificates of Pending Litigation and Construction Liens

You've likely heard the old saying that "you can't squeeze blood from a stone."

As you probably know, litigation is a lengthy, time consuming and expensive process. It can therefore be devastating to learn after years of litigation that an adverse party no longer has any money or assets to satisfy a judgment.

In certain disputes involving land, parties can take proactive steps to protect themselves from otherwise judgment proof debtors by securing an interest in the land, thereby preventing sale of the land during the litigation and forcing its sale to satisfy judgment. Two such tools are a Certificate of Pending Litigation and a Construction Lien. Each arises in different circumstances and carries its own benefits, requirements and limitations.

Certificates of Pending Litigation

In circumstances where there is a dispute over the ownership or title to land, a party claiming an interest in land may move before the Court and register on title a Certificate of Pending Litigation (CPL). The CPL may initially be obtained without knowledge of the owner, and will effectively prevent the owner from disposing of the property or even refinancing, since it is a notice to the world that the property is the subject of litigation. Once registered, the CPL can only be discharged from title on consent, upon resolution of the dispute, or if the Court orders its discharge.

A CPL is limited in that the registering party does not gain an interest in the land, whereas a Construction Lien actually gives the registering party an interest in the particular land in dispute.

Construction Liens

Generally speaking, where a party supplies services or materials as part of an improvement to a property and does not get paid, the party gains the right to register a charge (i.e. Construction Lien) against that property for the value of the service / materials supplied, which could ultimately (albeit rarely) result in sale of the property to pay the amount owing.

In order to gain the benefit of a Construction Lien, it must be preserved (i.e. registered on title) within 45 days of the last day worked / material supplied. In addition, within 90 days of the last day worked / material supplied, the lien must be perfected by the commencement of an Action and registration of a Certificate of Action on title. In turn, this action must be set down for trial within two years from the date of commencement of the Action. The lien will prevent the sale or refinancing of the property and will prevent any financial draws for ongoing construction until one of the following takes place:

A) the lien is vacated by one of the parties higher up the construction pyramid posting security into court. In this case, the lien, which previously was on title and attached to the property, is removed from the property and now attaches to the security posted; or,

B) the lien is discharged, meaning it is no longer on title or attached to the security. This is usually only after an agreement is reached between the parties or disposition of the court.

The Construction Lien can be a highly effective method of recovering debts in the right circumstances. However this process can become complicated when there are multiple lien claimants and competing interests.

Both CPL's and Construction Liens are powerful tools with far reaching consequences. However, they should not be used lightly as they can be scrutinized by the Court as well as opposing parties. For this reason, the Courts can impose severe costs consequences against the registering party in situations where the CPL or Lien is inappropriately registered. It is therefore recommended that you speak with litigation counsel before undertaking either of these potential remedies.

Case Comment: Acciona Infrastructure Canada Inc. v. Allianz Global Risks US Insurance Company, 2014 BCSC 1568

The August 19, 2014 decision of Acciona turns on the issue of coverage under a Course of Construction (COC or Builders Risk) Policy. The decision could be fundamental to the areas of construction and insurance law, and in particular the way in which the courts interpret the LEG2/96 clause – a design/workmanship – exclusion. Unfortunately, the case is currently being appealed and we will likely

not know its true impact for quite some time. The forgoing is unfortunate given that this area of the law is rarely commented on by the courts.

In Acciona, the Plaintiff was a joint venture Design/Build Contractor for a hospital extension located in Victoria BC. During construction, it was discovered that the concrete slabs in the extension were experiencing deflections. The Court determined that the cause of the deflection was the formwork and re-shoring procedures used during construction. Although structurally sound, significant remediation was required to meet the design intention.

The Plaintiffs claimed recovery for the cost of remediation under the COC Policy. The Insurers denied coverage and argued that (1) the slabs were defective and as such were not physically damaged, and (2) that based on the operation of the LEG/96 clause in the policy the issue fell under the "defects in material workmanship or design" exclusion.

LEG 2/96 model 'consequences' defects exclusion is worded as follows:

The insurer(s) shall not be liable in respect of all costs rendered necessary by defects of material workmanship design plan or specification and should damage occur to any portion of the Insured Property (Contract Works) containing any of the said defects the cost of replacement or rectification which is hereby excluded is that cost which would have been incurred if replacement or rectification of the said portion of the Insured Property (Contract Works) has been put in hand immediately prior to the said damage.

For the purpose of this policy and not merely this exclusion it is understood and agreed that any portion of the Insured Property (Contract Works) shall not be regarded as damaged solely by virtue of the existence of any defect of material workmanship design plan or specification.

The Decision

The Court held that the slabs were not in essence defective but were physically damaged by the formwork and re-shoring procedures (i.e. the process of construction). Notwithstanding that the plaintiffs' subcontractor constructed the slabs in the first place Skolrood J. found that the sagging and cracks fell within the perils insured clause as fortuitous damage. Consequently the Court held that the LEG2/96 clause did apply, as the covered "damage" consisting of over deflections and cracking of the concrete slabs, directly resulted from the improper formwork and shoring/reshoring procedures employed on site, which constituted a "defect in material workmanship".

Thus, pursuant to the LEG2/96 clause, the excluded costs would be those costs associated with remediation or rectification of the defect before the cracking and over deflections occurred.

Comment

On appeal it is uncertain how the interpretive reasoning of Skolrood J, will hold. First, the Court's reasoning can be interpreted to mean that a contractors own defective workmanship on an element of the project, which then subsequently results in damage to that same element, is excluded, but the resulting damage to that same element is not. This implies that for every defect/workmanship exclusion claimed by the insurer as a defence the courts will look to the construction process and determine, on a case by case basis, if the issue being denied coverage is itself the cause or the resulting damage within a single construction element. Given the nature of complex construction projects such an analysis could become very complicated.

Secondly, pursuant to the wording of LEG2/96, the excluded costs associated with remediating the damage are calculated based on what would have been incurred if replacement or rectification of the slab had "been put in hand immediately prior to the said damage." Putting same plainly, the excluded cost of the repair should be calculated the day prior to the damage (cracking and deflection) occurring. Hence, it can be argued that in this case if no repair was possible immediately prior to the damage, the excluded cost would have been that of repairing the entirety of the slab.

On the other hand, Skolrood J. held that the exclusion applied only to the increased costs which would have otherwise been incurred over time if the construction of the slab had been carried out correctly in the first place. In essence this would limit the exclusion to those costs associated with implementing proper formwork and shoring procedures to prevent sagging and cracked slabs throughout the construction process.

The difference in interpretation is critical given that if nothing could have been done to stop the cracking/deflection immediately prior to the damage, the excluded costs would be the entire cost of the slab repair, rather than the minor additional costs associated with doing the job correctly in the first place. It is for this reason that a decision from the appeal court will be instrumental in shedding further light on how the LEG2/96 clause, and clauses similar to same, will be interpreted in the future.

This article was originally prepared for and published by the Construction Law Section of the Ontario Bar Association, and was co-authored by Maxim Kaploun and Jeffrey A. Armel

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Service Outside of Ontario: Pitfalls and Lessons

In *Mitchison v. Zerona International Inc.,* 2014 ONSC 4738 the plaintiff brought an action in Ontario for damages against the defendant with respect to a franchise business purchased from the defendants. The

plaintiffs alleged the defendants violated the *Arthur Wishart Act (Franchise Disclosure)* 2000, S.O. 2000, C. 3. The statement of claim originally named Zerona Canada, carrying on business as Zerona International, as a defendant. Zerona Canada defended the action and pleaded that the impugned agreement was actually between the plaintiffs and Zerona International Inc. and another individual who was a director of Zerona International Inc. The plaintiff amended the statement of claim to add Zerona International Inc. as a defendant and corrected other misnomers in the title of proceedings.

Both Zerona International Inc. and one of the named individual directors of Zerona International Inc. resides in the Barbados. The plaintiff travelled to the Barbados and served Zerona International Inc. and one of the directors personally. The defendants were subsequently noted in default and thereafter brought a motion for determination that service of the amended statement of claim was invalid, as it did not comply with the requirements of the *Hague Convention on the Service Abroad of Judicial and Extra Judicial Documents in Civil or Commercial Matters, 15 November 1965*, Can. T.S. 1989 No. 2 ("the Hague Convention") and as such was not served in accordance with 17.05(3)(b) of the *Rules of Civil Procedure.* The defendants brought the motion without attorning to the jurisdiction of Ontario.

Master Glustein cited Article 10(c) of the Hague Convention which permits "any person interested in a judicial proceeding to effect service of the claim directly through the judicial officers, officials or other competent persons of the stated destination." Master Glustein determined that Article 10(c) precluded the "person interested in a judicial proceeding (i.e. the plaintiff) from effecting service himself. Accordingly, it is a requirement of the Hague Convention that service be affected through an intermediary rather than a litigant.

As a result, Master Glustein granted the defendant's motion, declared that the purported service of the claim was invalid, and set aside the noting in default of the Barbados defendants. This technical approach taken by Master Glustein led to a harsh result. The defendants were not denying that they received the claim or that they had timely notice of it. Nonetheless, Master Glustein was bound by the provisions of the Hague Convention and determined that service was invalid. This result would seem to be at odds with Rule 2.01 of the *Ontario Rules of Civil Procedure* which determines that a failure to strictly comply with the rules is an irregularity and does not render a proceeding or step in a proceeding a nullity. Nonetheless, it is important to realize that when engaging in cross-border litigation, it is imperative knowledgeable and experienced counsel be retained to handle such matters. Had the plaintiff in *Mitchison v. Zerona International Inc.* consulted appropriate counsel before serving the statement of claim personally, the cost, expense and delay associated with the motion could have been avoided.

Jeff Van Bakel practices in cross-border litigation, professional negligence defence and commercial litigation. He regularly ***blogs about cross-border litigation involving enforcing foreign judgments and letters rogatory here****.*

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