

GOVERNMENT

Lawyers outline biggest impacts from Construction Act changes

Angela Gismondi July 3, 2019



Practical solutions to changes in the new Construction Act with respect to commercial leases and tenant construction was the topic of a recent breakfast briefing, *Construction Issues in Commercial Leasing*, hosted by WeirFoulds LLP in Toronto.

“The single biggest impact on landlords that arise from changes to the Construction Act is the fact that the landlord might be held liable for 10 per cent of any payments it makes to the tenant on account of any improvements that are performed by the tenant in the premises,” explained Karsten Lee, partner, leasing law with WeirFoulds LLP.

Under the new act, the contractor has the right to lien against the tenant’s interest (leasehold interest) and the landlord’s interest (freehold interest) for 10 per cent of any amount payable by the landlord to the tenant for a tenant improvement. Landlords

should hold back 10 per cent of the tenant improvement allowance until the lien period expires, explained Lee. The deadline to register a lien has also changed from 45 to 60 days.

“ Landlords definitely need to pay attention to details ”

– **Karsten Lee**

WeirFoulds LLP

The main clause affected by the changes is the leasehold improvement allowance clause, which sets out the terms for which the landlord will pay the allowance to the tenant.

“While drafting these leasehold improvement allowance clauses landlords do need to keep in mind the changes that have been made to the Construction Act,” said Lee.

“Landlords definitely need to pay attention to details and all of these details need to be clearly and meticulously set out in the allowance clause in the lease.”

Lee said he has seen thousands of leasehold improvement allowance clauses over the years and unfortunately for many landlords, the wording in the clauses does not adequately protect them from the new changes in the Construction Act.

“I can’t tell you how many times I’ve seen an allowance clause simply state ‘landlord shall pay the full amount of the allowance to the tenant upon the tenant opening for business’ and it does not take into consideration the possible lien period and the holdback,” said Lee.

“Even worse, I’ve actually seen some allowance clauses over the years state that the landlord will pay the full amount of the allowance to the tenant before the work actually gets started... Unfortunately if the tenant ends up for any reason not paying its contractors then all of the sudden the contractor can come knocking on the landlord’s door and demand payment equal to 10 per cent of the allowance, this is even if the landlord already paid the full amount to the tenant beforehand.”

Faren Bogach, partner, construction law, WeirFoulds LLP, offered tips for dealing with liens in the commercial leasing context and common mistakes.

From a landlord perspective, one of the big mistakes is not holding back the 10 per cent.

“I have had cases where your tenant goes under you and can’t go after them, they’re bankrupt, and you have to pay that 10 per cent again so you want to make sure you hold it back,” said Bogach.

Another issue with landlords is where they become so involved in the construction project that they become a “deemed owner.”

“When a landlord becomes so involved that the contractor doesn’t even really know who they are dealing with...then the landlord may be deemed to be the owner and be responsible for everything and the contractor could lien for the full amount,” she explained.

“Make sure as a landlord you clearly have agreements to say what your relationship is. Don’t get involved to the point where you are essentially running the construction project for your tenant ... there should be that clear distinction between landlord and tenant.”

This can also happen to contractors who work on leasehold properties, explained Krista Chaytor, partner, construction and leasing law, WeirFoulds LLP.

“If you’re working for a tenant then you have to make sure you understand exactly what your rights are with respect to liens,” said Chaytor. “You have a lien not on real estate, per se, but a lien on the lease and this is very important because if you name the wrong party or the wrong interest in your lien you can be completely out of luck and you lose your lien rights all together.”

Important details for drafting leasehold improvement allowance clauses

TORONTO — At a recent panel discussion on Construction Issues in Commercial Leasing, hosted by WeirFoulds LLP, Karsten Lee, partner, leasing law, WeirFoulds, shared four details landlords should pay attention to when drafting leasehold improvement allowance clauses under the new Construction Act.

The first detail is what amount needs to be held back. Since the landlord is liable for at least 10 percent of the amount of the allowance then the holdback amount should be at least 10 per cent of the total value of the allowance or more if landlords are concerned about any rent-free periods or other payments being classified as “payment” made to the tenant in connection with the construction of its premises, he noted.

The second detail is how long you should hold back that amount. Under the new act it’s 60 days from the date that the work was completed on the premises, Lee said, adding landlords should not pay the holdback amount until it can confirm the 60-day period has passed and no liens have been registered on title prior to the end of that period.

Related to that, the third detail is how does a landlord know when the 60-day period starts and ends. Typically, landlords can get a tenant to sign a statutory declaration stating the date on which the work was completed and the 60-day period starts from that day. He also recommended getting a statutory declaration from the tenants' contractor. For larger projects, the 60-day period starts the day a certificate of substantial completion is published.

"If you're getting dates from both the tenant and their contractor then there is little room for argument down the road," said Lee.

The fourth detail is that the landlord must confirm there are no liens registered on title at the end of the lien period. They can do so by pulling title to the property once the 60-day period has expired and checking to make sure that a contractor has not registered a lien on title, he said.

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