

PUBLICATION

The Importance of Maintaining a Builder's Lien Holdback

Mark Rathwell

April 7, 2017

Contemplating a Renovation or Building Project? The Importance of Maintaining a Builder's Lien Holdback

As a property owner who is planning a construction project of any scope or magnitude, it is crucial to understand the concept of, and to maintain, a builder's lien holdback.

Imagine that you have just completed a \$200,000.00 renovation to your basement. You hired a general contractor who you trusted, and you are delighted with the results. You have paid the general contractor in full. Two weeks later, you receive, in the mail, notification from the Land Titles Office that three builders' liens have been filed in the total amount of \$60,000.00 by subcontractors who were hired by your contractor, but who were not paid by your contractor. Meanwhile, your contractor has disappeared off the face of the earth, or is otherwise bankrupt or insolvent.

Under normal principals of contract law, the subcontractors would have no legal remedy against you, as you did not contract with them directly. However, in most jurisdictions, including Alberta, legislation has been enacted to provide statutory remedies to unpaid contractors who have improved a property by furnishing labour or materials.

The unpaid contractors' recourse to the owner is not absolute, but limited to its proportionate share in what is known as a "lien fund". A lien fund consists of 10% of the value of the work actually performed on a contract, plus any amount which the owner owes to the general contractor which has not been paid. Using the example above, the lien fund would consist of 10% of the \$200,000.00 contract value, or \$20,000.00. As the owner has paid the general contractor in full, no additional amounts are added to the lien fund. Accordingly, the owner's total liability to the lienholders would be \$20,000.00. In most cases, all of the liens, regardless of their combined total amount, can be removed by paying that amount.

It is hard for many property owners to comprehend why, when they have paid their general contractor in full, they would be required to pay additional amounts to clear builders' liens. They have done nothing wrong. The answer to that question is the concept of the lien "holdback". Most construction contracts, regardless of their scope or magnitude, contemplate payment to the general contractor in phases or draws upon completion of various stages of construction. Using our example, it would be common for the \$200,000.00 to be paid, pursuant to the general contract, in five progress draws of \$40,000.00, each throughout the course of construction. The Builders' Lien Act not only permits, but obligates an owner to maintain a 10% holdback on all

sums paid to the general contractor throughout the course of construction. Again, using our example, if the owner withholds 10% (or \$4,000.00) on each of the five \$40,000.00 progress payments made throughout construction, the total holdback maintained by the owner, upon completion of the contract, should be \$20,000.00.

Upon completion of their work, contractors have 45 days in which to file a builders' lien if they have not been paid. Consequently, an owner should maintain, and withhold, the 10% holdback from the general contractor until 45 days have passed since the contract was completed, and no liens have been filed. If no liens have been filed by that time, the holdback can be released to the contractor with peace of mind that no liens will be registered.

Alternatively, if liens have been filed, the \$20,000.00 holdback can be used to clear all liens registered against title irrespective of the combined total sum of them. In either case, unlike the example noted above, the owner has paid no more money than he was obligated to pay in any event.

The moral of the story is simple - maintain a 10% holdback on all progress draws paid to your contractor. Do not release that money to the contractor until 45 days have passed since the completion of construction and no liens have been filed. For obvious reasons, many contractors do not like the application of a holdback, and they will rarely educate an owner on their right to maintain a holdback, or volunteer to be paid subject to a holdback. Nonetheless, it is your statutory right to maintain the holdback, and it is critical that you do so to avoid paying more than you bargained for.

For further information, please contact the author, Mark Rathwell at 403.225.6419 or any member of our Construction Litigation group.