

Litigation Points In Construction Contracts

Melvin L. Rothman *

Introduction

By way of introduction to the general nature of Construction Contracts and the sources of law thereon, one might recall that these contracts fall into the general category of "lease and hire of work". Article 1666 C.C. speaks of three principal types of work that may be leased or hired, the third item of which is "builders and others who undertake work by estimate and contract".

Construction Contracts are, of course, subject to the general rules of contract contained in the Civil Code, but in addition, they are subject to certain special rules as laid down in Article 1683 C.C. and following.

Independence of Contract

One of the essential features of the Construction Contract is the independent status of the contractor; unlike an employee in a contract of lease and hire of services, the contractor is not subject to the direction and control of the owner. He is free to choose, supervise, and dismiss his own employees and do the work as he sees fit so long as he completes it in accordance with the plans and specifications. One very important consequence of this independence is that the owner is not vicariously responsible in delict for any damage that might be caused by the fault of the contractor or any of his employees. Since the contractor is not an employee, Article 1054 C.C. does not apply. The owner could be responsible under 1055 C.C. but here it would have to be established that the damage was caused by the "ruin" of the building and this is often difficult to establish.

In *Quebec Asbestos Corp. v. Couture*,¹ the owner was sued in delict for damages caused by the fault of one of the contractor's employees. The Supreme Court dismissed the action basing itself on the complete lack of subordination that existed between the con-

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¹ [1929] S.C.R. 166.

tractor and the owner. The judgment lays down some of the guide lines for determining the existence of a "contrat d'entreprise" — no subordination, freedom to choose and supervise employees, payment for work and not time, etc.

Form

As to the form of building contracts, in *Bolduc v. Houle*² it was held that no particular form is required and the contract may even be verbal, subject of course, to the problems of proof one can have with verbal contracts. Certainly, verbal proof can be made against a contractor or sub-contractor to prove the contract itself since they have been held on many occasions to be "commerçants", but the contractor might have difficulty proving a verbal contract against the owner, and as will be seen, there are certain strict requirements against proving "extras" without a writing.

Extras

One of the most frequent problems in construction contracts is the problem of extras. Article 1690 C.C. provides that whenever a builder or architect undertakes a job upon plans and specifications at a fixed or lump sum price he cannot claim any additional sum on grounds of any changes in the plans or specifications or any change in the cost of labour or materials unless such change is authorized in writing or unless he can obtain an admission under oath from the owner. The purpose of this article is to protect the owner from any fraudulent or unwarranted claims by the contractor.

There are a great many cases on this article, most of which make it quite clear that it is imprudent for the contractor to proceed with any deviation from the plans without written authorization. But the article has been given a restricted interpretation on occasion. In *Tetrault Freres v. Nantel*,³ the Quebec Court of Appeal held that this requirement of Article 1690 does not apply where there are no plans and specifications, even where a fixed price has been agreed upon in the contract. Similarly, in *Leblanc v. Côté*,⁴ Article 1690 C.C. was again restrictively construed. The contractor had agreed to build two stories with the second story left unfinished. After the work had started, the owner instructed him to finish the second story. The court held that this was neither part of the contract, nor an extra, but a new agreement.

² [1962] C.S. 416.

³ [1959] B.R. 339.

⁴ [1943] C.S. 351.

In *Towstuck v. Brisebois*⁵ it was held that in the absence of a writing, a specific admission is required for each item of extra work. A general admission or a "commencement of proof in writing", would not be enough. Once the owner admits he authorized the extra, however, the proof as to value can be made according to the ordinary rules of law.

In *Eastern Constructors Ltd v. City of Montreal*⁶ the contractor encountered soil conditions different from those described in the plans and specifications. He did considerable extra work and claimed an increase in price. The court said he should have stopped work as soon as he found the new soil condition, notified the owner and obtained written authorization before proceeding, or asked to have the contract set aside on grounds of error. Not having done so, he was subject to 1690 C.C. — no extra.⁷

In *La Cie de Construction et de Bois de Ste-Agathe v. Dame Lambert*,⁸ it was held that errors in calculation by the contractor do not justify any increase in the contract price.

In practice, changes and extras are often authorized by the architect in issuing a "change-order" or certificate, and this would be binding on the owner as long as the architect has general or specific authority from the owner for this purpose.⁹

As to the position of sub-contractors under Article 1690 C.C., there are several cases which have held that the requirement of a writing for extras does not apply to extras ordered by the general contractor from a sub-contractor, that both parties here are merchants who know the trade and that the general contractor is not entitled to the same protection as an owner.¹⁰ But what happens if the relations between contractor and sub-contractor affect the owner? In *Gravel v. Diana Construction*¹¹ the general contractor had verbally authorized a sub-contractor to do certain extras. The sub-contractor registered a privilege for the amount of these extras against the owners' property, and the court held that 1690 C.C. applied to sub-contractors as well in this case; otherwise the owner

⁵ [1948] B.R. 292.

⁶ (1936) 74 C.S. 196.

⁷ See also *Paradis v. The King* [1942] S.C.R. 10, although in this case, the court decided not on the basis of Article 1690 C.C. but on a specific clause in the contract which imposed an obligation on the contractor to investigate soil conditions.

⁸ (1919) 56 C.S. 239.

⁹ *Bayard v. Drouin* (1902) 22 C.S. 420.

¹⁰ *Bouchard v. Lorion* (1938) 44 R.L.n.s. 325; *Mackay v. Davy* (1930) 36 R.L.n.s. 140.

¹¹ [1961] C.S. 476.

would lose all his protection. The contractor could have all of the work performed by sub-contractors and prove unauthorized extras this way that ordinarily would not be admitted.

Payment of Price - Malfaçons

What remedies are open to the owner where the contractor has not done the work according to his contract? Can he refuse to pay the price? Here is another great area of litigation and several distinctions must be made. Often these are very fine distinctions and sometimes their practical application has been confusing. In essence, the contractor's right to demand payment and the nature of the procedure he must adopt will depend on whether the work has been substantially completed.

It is a general principle in the law of contracts that a party cannot demand performance by the other party unless he has fulfilled his own obligations. The owner is entitled to withhold payment and the contractor cannot demand payment until the work has been substantially completed. Moreover, as long as there is a contract between the parties, the contractor cannot simply claim on a *quantum meruit* basis or on an unjustified enrichment basis. Since there is a contract, the contractor must show that he has fulfilled his own obligations thereunder.

In *Verona Construction Ltd. v. Frank Ross Construction*¹² a sub-contractor abandoned the work because he had encountered quicksand and the general contractor was not willing to agree to an increase in price. He then sued for the balance of price for work he had done and the owner counter-claimed for damages because of the abandonment. The Supreme Court found that the abandonment was not justified and held that since he had not completed his contract he could not ask for any payment.

Similarly, in *Bertheau v. Gagnon*,¹³ the court found that the work had been done so badly that the owner had to redo a great deal of it and the owner was justified in refusing payment. The contractor had not substantially fulfilled his own obligations and this was a good defense to the action. There was no need for cross demand.¹⁴

On the other hand, there are many instances where the contractor has substantially completed the contract, but there may remain certain "malfaçons" or minor items to complete or repair. In these cases, the contractor is entitled to claim payment and if the

¹² [1961] S.C.R. 195.

¹³ [1959] B.R. 473.

¹⁴ See also *Anctil v. Côté* [1950] C.S. 461.

owner has any claims for "malfaçons", he must assert these not by defense but by cross demand so that he can have them liquidated.

The distinction between "malfaçons" and inexecution of a contract was made as follows by Mr. Justice Letourneau in the case of

Morissette v. Beaudette:¹⁵

"Cet appel nous met d'abord en présence de la distinction qu'il convient de faire entre une malfaçon et l'inexécution . . .

Il me paraît certain que dans un cas de contrat à forfait, l'entrepreneur ne peut en principe être payé que s'il a substantiellement exécuté son contrat et chacun des items de son contrat: *non adimpleti contractus*. Par contre, s'il est *prima facie* établi, par acceptation ou autrement, que les travaux ont été complétés, le droit à la créance existe, sauf pour le débiteur à faire valoir des déductions à raison de malfaçon ou un remboursement quant à des réfections; si le constructeur n'a pas complété substantiellement son ouvrage, il ne peut prétendre à son paiement et c'est par défense qu'il faut lui opposer ce moyen; mais si, ayant complété substantiellement son ouvrage, d'après une preuve *prima facie* suffisante, il se trouve que le propriétaire veut réclamer pour malfaçons ou réfections, c'est à la demande reconventionnelle que ce dernier devra recourir."

In the *Morissette* case, the contractor was claiming a balance of price of \$1,950.00 due under a contract for construction of a house which he alleged had been completed, occupied and accepted by the Defendant. The owner contested the action by defense, claiming that the balance was not due in that certain work had yet to be completed. For this type of situation the court held that a defense was not the proper remedy and that any such claims by the owner would have to be asserted by cross demand.¹⁶

The new Code of Procedure will probably simplify the problem considerably in doing away with the necessity for a cross-demand in these cases. But until then, the *general rule is that as long as the contract has been substantially completed or the work accepted — any claim for "malfaçons" must be made by cross-demand*. The usual procedure for the owner is to put the contractor in default to do the repairs and if these are not done, he has the work done by another. Then when he is sued for the balance of price, he claims the cost of repairs by cross demand, and asks for compensation against the price claimed by the contractor.

"Acceptance" of the work by the owner normally means that the work has been substantially completed and the contractor can claim his price. It may also mean that the owner has acquiesced in the

¹⁵ (1928) 45 B.R. 73 at 79.

¹⁶ See also *Laplante v. Hamelin* [1957] B.R. 417; *Chouinard v. Best-Ever Footwear* [1961] C.S. 641; *Duelz v. Kajandi* [1960] C.S. 89.

“malfaçons” and will not be able to complain about them.¹⁷ Acceptance may be express or tacit. In *Lebel v. St-Georges*¹⁸ the owner had watched the work throughout and was well aware that the contractor had deviated from the plans in the floor level. He could not later complain of this as a “malfaçon”. But the mere fact of taking possession of the building by the owner or his making payment under the contract does not always mean he has accepted, particularly where the defects are not readily apparent.¹⁹

Cancellation of Contract

Article 1691 C.C. provides another exception to the general law of contracts. Normally, of course, a contract cannot be cancelled without the consent of both sides; but under Article 1691 C.C., the owner has the unilateral right to cancel a fixed price building contract at any time, even after the work has begun, on indemnifying the contractor for all his labour and expenses and paying damages according to the circumstances.

The right of the owner to cancel is quite clear under Article 1691 C.C., and it is equally clear that contractor must be paid all of his expenses for labour and materials. The question of what damages or loss of profits the contractor can claim has been somewhat less clear, however. In *Tremblay v. Charest*²⁰ after cancellation of the contract, the contractor simply claimed the price under the contract, offering to complete same but made no proof of expenses or damages. His action was dismissed.

In *Tidewater Shipbuilders v. Naphtes Transport*,²¹ the Supreme Court held that the right of the contractor to be paid expenses of labour and material was absolute, but his right to damages would depend on the circumstances of each case. The contractor is not entitled to payment as if the contract had been executed and he cannot claim the profits he would have obtained had the contract not been cancelled. He should be able to claim any profits which he lost on other contracts because of taking this job.²²

¹⁷ *Emond v. Saad* (1927) 65 C.S. 188.

¹⁸ [1961] C.S. 66.

¹⁹ For a more detailed study of “acceptance” see Walter Johnson, *The Redhibitory action and buildings — Implications of acceptance of work* (1952) 12 R. du B. 322.

²⁰ [1963] C.S. 587.

²¹ [1927] S.C.R. 20.

²² *Auclair v. Brownsburg* [1946] B.R. 466 is to the same effect. It also deals with an interesting question as to whether an accepted tender constitutes a contract.

In *Gauthier v. St. Laurent*,²³ it was held that a contractor could claim no loss of profits where the contract was cancelled before the work was started, where he had incurred no expenses, had not missed any other contracts and had not tried to get any other work since cancellation.

Article 1691 C.C. gives the owner the right to cancel, but this article does not apply as between the general contractor and subcontractor,²⁴ and here cancellation requires mutual consent. Therefore, the subcontractor should be able to claim not only his expenses but all profits he would have made had the contract not been cancelled. Presumably these would be reimbursed to the general contractor by the owner.

Article 1691 C.C. does apply to architects as well as builders, however. In *Hôpital St. Luc v. Beauchamp*²⁵ the architect had been retained to prepare plans and supervise work. After only part of his work was completed, the hospital cancelled and retained another architect. He was awarded damages equivalent to the fee according to tariff on the completed work and something for the balance of the work as well.

Finally, a clause in the contract allowing the owner to cancel with no indemnity at all is legal and not contrary to public order.²⁶

Risk and Insurance

As to the risk of loss or damage by fire or otherwise during construction, Articles 1684, 1685 and 1686 C.C. cover this contingency. Generally, if the contractor furnishes labour and materials at a fixed price, the loss of the thing in any manner whatsoever before delivery falls upon the contractor, unless the loss has been caused by the fault or default of the owner. If the contractor furnishes labour only, unless he is proved to be at fault, the loss falls upon the owner, but the contractor is not entitled to claim his wages.

It is certainly very important that proper arrangements be made under the contract for *insurance* during construction. In *Commissaires d'École de St-Eugène v. Baloise Fire Insurance*,²⁷ the owners and the contractors had each taken out separate policies, covering the building under construction. When a fire occurred, the owners

²³ [1958] B.R. 114.

²⁴ *Pelisson v. Desrochers* [1958] C.S. 289.

²⁵ [1950] S.C.R. 3.

²⁶ *Cambrai Construction Inc. v. Hospital St. Ambroise* [1963] S.C.R. 391.

²⁷ [1944] C.S. 19.

tried to recover under their own policy. The court held that the owners had no insurable interest because, until the completion and delivery of the building, the construction belonged to the contractor and any loss fell on him.

Most contracts require the contractor to maintain a satisfactory policy with loss payable to the owner and contractor "as their interests may appear".

Arbitration Clauses

Most contracts contain a clause to the effect that any disputes between the contractor and the owner or architect shall be settled by arbitration without recourse to the courts.

It is well known, of course, that such clauses can be of very doubtful validity and that if the clause constitutes a "clause compromissoire", it will not be enforced by the courts. The test of its validity seems to be whether or not the clause deprives the parties of their recourse to courts. Most of the clauses this author has seen in the standard contract are probably invalid.

On the other hand, if properly framed such clauses can be made to have some effect. In *Boisvert v. Plante*²⁸ the clause was to the effect that before any party took his dispute to court, he agreed to submit to arbitration. This did not deprive the parties of their right to go to court; arbitration was merely a condition precedent to the right of action and the clause was held valid. Since the action was taken without fulfilling this condition, it was held to be premature and dismissed.

Cost Plus Contracts: Keeping Records

Finally, a word on a very obvious but very important aspect of cost-plus contracts. Since the contractor here is paid on the basis of the actual cost of his labour and materials, he has a fiduciary obligation to keep full, detailed and accurate records of his costs. For materials, he must be able to show the actual cost of all materials used on the job. For labour, he must have detailed time records of all time spent and work done. Estimates are not enough.²⁹

²⁸ [1952] B.R. 471.

²⁹ *Fecteau v. Benn* [1958] B.R. 706; *Montreal Locomotive Works v. Black Clawson*, S.C.M. 451,399, now in appeal.