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# FROM THE GROUND UP

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## Unjust Enrichment and the Builder's Lien Claimant

by Kirk Lamb, Student-at-Law

### INTRODUCTION

Construction projects are often characterized by complex relationships among owners, general contractors, and subcontractors of any tier, including end sub-subcontractors and so on. In this way the services are performed and materials furnished by various persons. How do such persons protect or recover the value of the work provided or the materials furnished?

The first line of protection is to rely on contracts covering the services or materials. The second is to rely on builder's lien legislation to recover the value of the services or materials rendered. In many cases builder's lien legislation will provide an adequate remedy. However, this may not be true depending on the size of the lien fund and the lien claimant's diligence in satisfying statutory requirements. Is there another way at law to bring an action against the owner, or alternatively, the general contractor?

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## UNJUST ENRICHMENT

One possibility is an action known as an action for “unjust enrichment”.

In general, recovery for unjust enrichment will be permitted where the subcontractor can establish three general principles: (1) the enrichment of the general contractor; (2) a corresponding deprivation suffered by the subcontractor; and (3) the absence of any juristic reason to justify the enrichment. At first glance, a subcontractor that provides uncompensated for goods or services to a construction project may have a valid action for unjust enrichment against the general contractor or the owner. Indeed, the general contractor or owner has been enriched to the extent of the value of the goods or services and the subcontractor has been deprived of the same. However, Alberta case law suggests that the validity of unjust enrichment actions against general contractors and owners is questionable at best.

**Can a subcontractor with remedies available to it under builder’s lien legislation bring an unjust enrichment action against a project owner? No.**

### a. Alberta Decision

Master Funduk recently considered the issue in *624250 Alberta Ltd. v. Acklands-Granger Inc.* (“*Acklands-Granger*”).<sup>1</sup> In that case Eclipse Inline Rollerskating Recreation Centre Inc. (“Eclipse”) contracted 624250 Alberta Ltd. to perform work on property it was subleasing. After the work was completed, Eclipse refused to pay. The numbered company sued the owner of the property with which it had no contract, for unjust enrichment. In considering whether 624250 Alberta Ltd. could bring an action for unjust enrichment, Master Funduk considered the position of the subcontractor at common law. He pointed out that where the subcontractor has a contract with the owner then it has a remedy in the form of a lawsuit in debt or in contract. However, where the subcontractor does not have a contract with the owner, the subcontractor has no common law remedy against the property owner—a troublesome situation since it is the owner that will ultimately benefit from the subcontractor’s uncompensated work. Master Funduk recognized this gap in the common law but failed to allow an unjust enrichment claim to fill it. Instead, he reasoned, the legislature addressed the gap when it provided lien remedies to subcontractors under the *Builders’ Lien Act* (“the *Act*”).<sup>2</sup> It would not be appropriate, reasoned Master Funduk, to hold the owner personally liable to contractors for unjust enrichment when the legislature had addressed the gap in the common law.

### b. Decisions in Other Jurisdictions

This judicial view of the matter in Alberta is supported by decisions in other jurisdictions. The Supreme Court in British Columbia in *A & D Masonry Ltd. v. Elbee Development Corp* (“*Elbee*”)<sup>3</sup> held that where a party has remedies available under builder’s lien legislation it would be inappropriate to also allow actions based on unjust enrichment. To this end the Court stated that the legislature, through the builder’s lien legislation, provided a remedy for subcontractors and to extend the remedy of unjust enrichment to the relationship

between the subcontractor and owner would be an unwarranted intrusion into the construction field. In *Elbee*, the subcontractor had contracted with the general contractor, not the owner. Its remedies lay against the general contractor in an action for contract or against the property pursuant to the builder’s lien legislation.

The Ontario Superior Court of Justice also held that the plaintiff’s claim for unjust enrichment could not succeed because the builder’s lien legislation in Ontario provided a remedy.<sup>4</sup> The Court stated that the legislature provided a contractor with a remedy against an owner and, if the contractor chooses not to seek recourse under the builder’s lien legislation, it cannot thereafter seek recovery on the basis of unjust enrichment

**Can a sub-subcontractor with remedies available to it under builder’s lien legislation bring an unjust enrichment action against a general contractor? Maybe.**

### a. Recent Alberta Decision

This question was most recently explored in Alberta in the case of *Litemor Distributors (Edmonton) Ltd. v. Midwest Furnishings & Supplies Ltd.* (“*Litemor Distributors*”).<sup>5</sup> In *Litemor Distributors*, Midwest was the general contractor for the construction of a hotel and Leland was the electrical subcontractor working under Midwest. Litemor, the plaintiff, was a sub-subcontractor, supplying light fixtures to Leland. Leland sought to have the fixtures supplied by Litemor on credit. Litemor did not consider Leland to be an acceptable credit risk. Because Leland was not an acceptable risk, Midwest, the general contractor, submitted a credit application to Litemor in order to get Litemor to supply the fixtures. Litemor agreed and invoiced the general contractor, Midwest, directly. When Leland then went into receivership, Litemor contacted Midwest for payment of the invoices. Midwest refused to pay. In response to Midwest’s refusal, Litemor brought an action against Midwest for breach of contract, and alternatively, for unjust enrichment. The Court held that there was no contract between Litemor and Midwest, only between Litemor and Leland. It then went on to determine whether Litemor could maintain a claim against Midwest for unjust enrichment.

### b. Application of the Criteria

The Court applied the three criteria for unjust enrichment and found that Midwest was *enriched* when Litemor provided the fixtures because Midwest was able to pass on a completed project to the owner. In terms of the second test, the Court found that Litemor suffered a corresponding *deprivation* in that they purchased the fixtures from their supplier and delivered them to the hotel at their own cost. The third test—absence of any juristic reason for the enrichment—required more consideration. Midwest argued that there was indeed a juristic reason to deny recovery: to permit recovery by Litemor would be contrary to and subvert the legislative scheme established by the *Act*. They argued that the purpose of the *Act* is to regulate the construction industry and that it is a complete code governing the relationship between all owners, contractors and sub-contractors.

Relying on an unjust enrichment action for protection in the event of non-payment for service or goods provided is a tenuous position for the construction subcontractor.



Madam Justice Read disagreed. She noted that the purpose of the *Act* is to protect owners, not contractors, from personal liability except to the extent of the lien fund, with all the liability-limiting provisions for the benefit of the owner. The *Act* does not speak to remedies against the general contractor and does not, therefore, disable sub-subcontractors such as *Litemor* from suing the general contractor. The Court then considered the unjust enrichment action on its merits and held that there was no juristic reason to justify the enrichment of *Midwest*. Thus the claim by *Litemor* for unjust enrichment against the general contractor was allowed.

### c. Caution with the Decision

One ought to be cautious in reading the decision in *Litemor Distributors* too broadly. *Litemor Distributors* presents a unique set of facts in that the general contractor introduced itself into the relationship between *Litemor* and *Leland* by negotiating with *Litemor* and applying for credit. Madam Justice Read relied heavily on the dealings between *Midwest* and *Litemor* in allowing the claim for unjust enrichment. Indeed, some judges and scholars believe that in order for an unjust enrichment action to be maintained there must be a “special relationship” between the parties, which makes it “unjust” for the defendant to retain the benefit. The Ontario Court of Appeal explained that this relationship is usually

marked by two characteristics, first, knowledge on the part of the defendant of the benefit, and second, either an express or implied request by the defendant for the benefit, or acquiescence in its performance.<sup>6</sup> Other judges and scholars, including Madam Justice Read in *Litemor Distributors*, simply ask whether the defendant’s conduct was the “proximate cause” of the plaintiff performing the service or furnishing the materials.<sup>7</sup> Madam Justice Read, in allowing the action for unjust enrichment, pays particular attention to the interaction between *Midwest* and *Litemor* as well as to *Midwest*’s conduct during the course of the project. Whether framed as “special relationship” or whether framed as “proximate cause”, these unique facts significantly influenced Madam Justice Read’s decision to allow unjust enrichment.

Does the absence of a “special relationship” or conduct by the contractor causing the sub-subcontractor to provide the goods or services prove fatal to an action for unjust enrichment? Perhaps not, however, the difficulty in any such action will be that in the commercial context the correct application of the three unjust enrichment criteria focuses on the “unjust” element of unjust enrichment and the standard of fairness is that of “commercial good conscience” and “honest” dealing.<sup>8</sup> This has effectively raised the bar for claiming unjust enrichment in the commercial context since enrichment resulting from honest, fair dealing is not unjust and will not attract a restitutionary remedy. The issue then becomes, will a court find an enrichment to be “unjust” in the absence of special relationship or causal conduct by the general contractor? Establishing injustice in the absence of a special relationship or proximate cause presents a significant hurdle to any unjust enrichment action in the commercial context—especially where the general contractor has no dealings, interaction or relationship with the sub-subcontractor.

## CONCLUSION

Relying on an unjust enrichment action for protection in the event of non-payment for service or goods provided is a tenuous position for the construction subcontractor. There appears to be little room for unjust enrichment actions against the general contractor, and even less room for such actions against the owner. Since subcontractors will face some hurdles in relying on unjust enrichment for compensation for goods or services, they ought to ensure that where possible the value of the goods or services be protected by contract. In addition, subcontractors ought to make sure that they comply with the requirements of the *Act* thereby maintaining any available lien remedies.

## Footnotes

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- <sup>1</sup> 2002 ABQB 533 (Master)  
<sup>2</sup> R.S.A. 2000, c. B-7  
<sup>3</sup> (1999), 49 C.L.R. (2d) 214 (B.C. Sup. Ct.)  
<sup>4</sup> *Elmford Construction Co. v. South Winston Properties Inc.* (1999), 45 OR (3d) 588 (Ont. Sup. C.J.) at para. 36  
<sup>5</sup> 2007 ABQB 23  
<sup>6</sup> *Nicholson v. St. Denis* (1975), 57 D.L.R. (3d) 699 (Ont. C.A.) at para. 8 adopted in *Alberta in Agrium Inc. v. Chubb Insurance Co. of Canada*, 2002 ABQB 495 at para. 32  
<sup>7</sup> *Litemor Distributors*, para. 34  
<sup>8</sup> *Atlas Cabinets & Furniture Ltd. v. National Trust Co.* (1990), 45 B.C.L.R. (2d) 99 (B.C.C.A.) at paras. 32 and 36



# Liability of Design Professionals to Third-Party Contractors

by Aaron Grach, Student-at-Law

## INTRODUCTION

This article is a refresher on a 15-year-old Supreme Court of Canada (“SCC”) case on the liability of design professionals to third-party contractors who rely on the designers’ work. The case reaffirmed the principles of the tort of negligent misrepresentation, and continues to have significant implications for risk management on the part of design professionals.

The case is called *Edgeworth Construction Ltd. v. N.D. Lea & Associates Ltd.*<sup>1</sup> (“*Edgeworth Construction*”). In it, the SCC considered the liability of an engineering firm to the contractor who bid on a contract based on the engineering firm’s design, and then suffered economic losses when the design proved inadequate. The SCC awarded damages to the contractor, even though there was no contract between the contractor and the engineering firm.

The plaintiff in the case was the construction firm Edgeworth Construction Ltd. (“Edgeworth”), which was in the business of building roads. Edgeworth bid on a contract with the Ministry of Highways (“Ministry”) to build a section of highway in the Revelstoke area of B.C. It won the bid and completed the work, but claimed that it suffered economic losses due to errors in the specifications and construction drawings. Those specifications and drawings had been prepared by the engineering firm of N.D. Lea and Associates Ltd. (“N.D. Lea”).

There were two complicating factors in the case. One was that Edgeworth and N.D. Lea did not have a contractual relationship between them that would have set out the terms of their relationship and entitled either party to sue the other for breach of those

terms. Instead, as is commonly the case, there were two separate contracts with the Ministry, one between the Ministry and N.D. Lea for the engineering work, and another between the Ministry and Edgeworth for the actual road building. The other relevant factor was that the building contract had a disclaimer protecting the Ministry from errors in the engineering specifications. The contract said that the specifications were provided only for the “general information of bidders”, and that any representations in the tender documents were not warranted or guaranteed by the Ministry.

The issues, then, were whether Edgeworth could still bring an action against N.D. Lea in spite of the lack of a contract between them, and whether Edgeworth could succeed in that action in the face of the Ministry’s disclaimer.

## NEGLIGENT MISREPRESENTATION

Edgeworth based its case against N.D. Lea on the tort of negligent misrepresentation, the principles of which were set out in the 1964 English House of Lords decision of *Hedley Byrne v. Heller*<sup>2</sup> (“*Hedley Byrne*”). That case said that liability arises when a person or company exercises skill or judgment to provide information, knowing that another may rely on that information, and the other does in fact rely on the information and suffers a loss because of that reliance. The person providing the information must exercise due care, and not be negligent, in making its representations. This duty of care arises independently of any contractual relationship between the parties. In *Edgeworth Construction*, the contractor claimed to have foreseeably and reasonably relied on the engineer’s specifications and drawings in making its bid, and then suffered losses when the engineering work turned out to be flawed.

## THE ENGINEER’S ARGUMENTS

N.D. Lea argued that any duty of care it owed to Edgeworth was negated by Edgeworth’s contract with the Ministry. The engineering firm maintained that the only way for Edgeworth to bring a claim for design defects was for the builder to sue the Ministry in contract, letting the Ministry then claim over against the engineers. N.D. Lea also argued that the existence of such a contract should annul any duty owed in tort.

## SUPREME COURT DECISION

If Edgeworth were restricted to suing in contract, it could indeed only sue the Ministry. However, the SCC rejected this notion. The court followed *Hedley Byrne* in holding that plaintiffs may sue concurrently contract and tort, provided that no contract explicitly negates the imposition of a tort-based duty of care.

The SCC held that the Ministry’s disclaimer protected only the Ministry, it did not protect N.D. Lea. Moreover, the fact that there was no contract between Edgeworth and N.D. Lea also did not protect N.D. Lea. Instead, it cleared the way for the negligence claim. So, while Edgeworth had no basis to proceed against N.D. Lea in contract, it could still proceed in tort.

In the end the tort claim was successful. The SCC held that it was reasonable to assume that bidders would rely on the engineering documents provided, not only for making their bids, but also for doing the actual construction work. Because of the typically short amount of time allowed for filing tenders—in this case about two weeks—a contractor could not be expected to conduct an independent review of engineering work that may have taken years to complete.

The SCC also noted that it made “good practical and economic sense” for the engineering firm to be responsible for the adequacy of its design. Although this assumption of liability risk might make the engineering services more expensive, it would cost even more to have the same engineering work done over again by each bidder—a cost that would, in the case of road building, be incurred by the taxpayer.

## LIMITING LIABILITY

The SCC noted that N.D. Lea could have taken measures to limit its liability. For example, the engineering firm could have put a disclaimer of responsibility on the documents relied on by the bidders. It could also have insisted on an ongoing supervisory role in the construction project, allowing it to alter the design as necessary as the construction progressed. Finally, it could have accepted the risk of tenderers relying on its work, and insured itself accordingly.

## INDIVIDUAL ENGINEERS NOT LIABLE

Interestingly, although the SCC found the engineering firm in *Edgeworth Construction* liable as a whole, it did not hold the individual engineers responsible, even though the engineers had put their personal seals on the drawings in question. The SCC said that a seal itself was not a guarantee of accuracy, but only a means to certify that a professional engineer had prepared the document. In this case Edgeworth had not relied on personal guarantees by the engineers themselves, but on the character of the engineering firm as a whole. It was reasonable under the circumstances to assume that Edgeworth would also rely on the firm’s pocketbook, rather than the pocketbooks of the individual engineers.

However, in other circumstances it is possible for reliance to attach to the approving design professional. This may depend on

the character of the relationship between the design professional and the client, or on the special skill or qualifications of the particular designer.


For example, in *Disal Contracting Ltd. v. J. Salamon Holdings Inc.*<sup>3</sup>, the court attached liability not only to the architectural firm, but also to the individual architect who had placed his seal on the construction drawings. This was because the plaintiffs had originally approached the individual architect, and notwithstanding the firm’s name on the contract, the work had proceeded with the understanding that the plaintiffs were the individual architect’s clients.

In *Boss Developments Ltd. v. Quality Air Maintenance Ltd.*<sup>4</sup>, the plaintiff bought an aircraft on an as-is-where-is basis. However, it was a condition of the sale that the aircraft be certified airworthy. Certification was obtained, as per Transport Canada’s regulations, based on a logbook entry that was signed and stamped by a particular aircraft maintenance engineer to signify that he had performed the requisite maintenance in accordance with standards of airworthiness. Neither the maintenance engineer nor his company were party to the contract of sale. The Court held that because the issuance of the certificate of airworthiness depended on the endorsement of a specific individual with specific skills and qualifications, it was clear that the buyer had relied on that individual’s endorsement.

## FURTHER CONSIDERATIONS

Thus, while the case of *Edgeworth Construction* has not been overruled, it may be distinguishable from other cases on the facts. Notably, in a twin decision on a case heard on the same day in 1993, the SCC declined to find the design professionals liable in negligence. The case was *Auto Concrete Curb Ltd. v. South Nation River Conservation Authority*<sup>5</sup> (“*Auto Concrete*”). In it the SCC held, in a short seven-paragraph decision, that where the method of doing the work is unspecified, it is up to the contractor to choose the appropriate method and to account for the associated risks and costs.

The contract in this case was for dredging a river. The contractor chose a suction method, not knowing that it would require permits that were hard to obtain, in contrast to the backhoe method used by contractors working on other sections of the river. When the contractor was



**A design firm providing specifications for a construction project must consider its liabilities. It is under a legal duty to exercise due care in ensuring that the design work meets professional standards of quality and accuracy.**

unable to obtain the necessary permits, it had to adopt other procedures and lost money. The contractor sued the engineers, alleging that they were negligent for failing to warn of the permit requirement.

The SCC held it to be a well-settled matter of law that where the choice of work method was left open, it was not up to the engineers

to advise the contractor of the risks involved in the work method actually chosen. While some engineers might choose to give such advice, this did not impose a specific duty on others to do the same.

The decision in *Auto Concrete* was made without explicit reference to the general duty of care owed by the design professional

to the contractor. Instead the question was about the appropriate *standard of care*. As in *Edgeworth Construction*, there was no contract between the contractor and the engineers. Similarly also, the engineers had provided the specifications knowing that contractors would use them in calculating their bids. However, notwithstanding the general duty found in *Edgeworth Construction*, in *Auto Concrete* the SCC ruled that the professional standard of care that applied did not require the warning that the contractor claimed it was owed. Where the work method was unspecified, the contractor could make a choice, and in doing so must itself account for the risks involved.

## CONCLUSION

A design firm providing specifications for a construction project must consider its liabilities. It is under a legal duty to exercise due care in ensuring that the design work meets professional standards of quality and accuracy. This duty is owed to anyone the design firm knows may rely its work, including a third-party contractor.

However, what constitutes reasonable reliance, as well as what is the appropriate standard of care, will depend on the professional standards involved, and on the other circumstances of the particular case. Both design professionals and building contractors need to take the appropriate precautions.

In situations like in *Auto Concrete*, the contractor must account for the risks associated with the work method chosen. In situations like in *Edgeworth Construction*, a design firm might consider one of the options suggested by the SCC to limit its liability—a disclaimer, a continuing supervisory role or liability insurance.

Clearly the options available in each case will have differing degrees of protection, flexibility and financial efficiency. The choice may therefore be dictated by the circumstances of the project itself.

## Footnotes

<sup>1</sup> [1993] 3 S.C.R. 206

<sup>2</sup> [1964] AC 465

<sup>3</sup> (1997), 35 C.L.R. (2d) 200 (Ont. C.J.)

<sup>4</sup> (1995), 5 B.C.L.R. (3d) 209 (B.C. C.A.)

<sup>5</sup> [1993] 3 S.C.R. 201



## What We've Been Up To

John Taylor has co-written articles for Oilsands Review with Catherine Reyes, Jim Swanson, Michelle Forrieter and Patricia Quinton-Campbell. The articles were (respectively) "Watch What you Say: The Lesson from Klemke Mining Corporation & Shell Canada Limited et al", "Seven Myths about Email and Electronic Communications and Records", "Intellectual Property Development – A Cautionary Tale" and "Detailing the Athabasca River Water Management Framework". Oilsands Review is a monthly magazine published by JuneWarren Publishing to provide articles of interest to participants in oil sands' development.

Simon Lee and John Taylor presented topical issues with respect to the Law of Tendering at an in-house client luncheon seminar in January 2008.

John Taylor is preparing to present a session at the upcoming Canadian Institute Conference in Edmonton entitled "Negotiating Construction Contracts", scheduled for April 28, 2008.

The Construction Team would be pleased to customize any of our presentations or seminars to meet the needs of any of our clients who have sufficient interest to make a private seminar useful to them.



# Seven Myths about Email and Electronic Communications and Records

by James T. Swanson and John K. Taylor

Most companies have witnessed the volume of email and other forms of electronic communication (both internally and with external parties) grow exponentially over the past few years. Any of the projects developing the Oil Sands of Alberta use email to facilitate contracting, develop engineering documents, satisfy payments between parties and exchange claims, some of which evolve into full litigation. The volume, diversity and importance of correspondence now being exchanged by email and other electronic means has resulted in a variety of statutes to address such communication but, for the most part, the “legalities” surrounding electronic communication are very similar to those with respect to “paper” correspondence. None of the myths outlined below is unique to people participating in the development of the Alberta Oil Sands but each of them, hopefully, will shed some light on how well (or poorly) your management of such correspondence is based on proper assumptions.

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## MYTH #1:

*Email is not legal correspondence.*

**FACT:** Email is like any other correspondence. It may have legal effect depending on the intention of the writer as expressed in the document, as well as on the intention of the recipient as expressed in any reply. There may be issues proving who authored an email, or whether or not it was received, but those can generally be dealt with, and there are legal mechanisms to do so.

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## MYTH #2:

*Contracts cannot be made by email or other electronic communications.*

**FACT:** Someone should tell eBay and Amazon. To be binding, contracts require an offer, an acceptance and consideration, which means something of value being exchanged. Alberta and all other provinces, as well as the federal government, have legislation enabling electronic contracting and transactions. If it is clear from communications that the parties intended a legal consequence, the courts will enforce any resulting agreement.

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**MYTH #3:**

*A contract written on paper cannot be varied or terminated by email or other electronic communication.*

**FACT:** See Myth #2 above. There may be cases where a paper agreement contains a provision stating that it cannot be varied by email, and that may well be enforceable, but, without such a provision, the courts will look at the intention of the parties to a communication to determine whether there was an intention to give legal effect to the communication. This is more likely in circumstances where one party may have acted in reliance on the communication. Many change order procedures we see do not account for these matters well.

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**MYTH #4:**

*An electronic document has no legal effect as a record unless we formally say it does.*

**FACT:** Alberta's Rules of Court and Alberta's Evidence Act, as well as similar legislation in other provinces, provide that a record is essentially anything that can be perceived by sight, sound or both. Under legislation in effect in all provinces, an electronic record, with some exceptions such as wills, codicils and transfers of land, will not be denied legal effect simply because it is in electronic form. In addition, most paper records now begin their existence as electronic records, only becoming paper when the electronic version is printed. Many documents in electronic form are never printed at all. Many potential records, particularly in the context of litigation, may be created by computers without direct human involvement at all, but they are still records and, if relevant, must be disclosed in litigation.

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**MYTH #5:**

*There is no obligation to preserve electronic records, including emails.*

**FACT:** There are legal obligations to preserve certain types of information and records, and whether or not those are in electronic form is generally not relevant. If an email is a financial record under legislation like Sarbanes Oxley, and it may well be, then destroying the email will be a criminal offence. Other requirements to preserve records arise under many pieces of legislation and regulations, including the Income Tax Act and the Employment Standards Code. In addition, there are obligations in situations where litigation is known to be pending or where litigation has been filed to preserve all relevant records, and this typically includes emails as well as other electronic documents. The cost and time to sort through poorly catalogued records that can number in the tens or hundreds of thousands for an average commercial claim of any complexity can be huge. Are you prepared?

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**MYTH #6:**

*It is easy to permanently delete electronic documents and records, including emails.*

**FACT:** While electronic documents are in many ways very fragile, the manner in which the technology operates generally creates multiple copies in separate locations. In addition, recovering deleted information, including fragments of information that may have never been part of a formal document, is generally a comparatively simple manner if the right software is used. Keep in mind that, once an email is sent, it can be forwarded and copied endlessly. Once sent, the sender loses control over an email message and, even if successfully deleted on the sender's personal computer, the mail server and the recipient likely still have copies.

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**MYTH #7:**

*We are best off to just keep everything.*

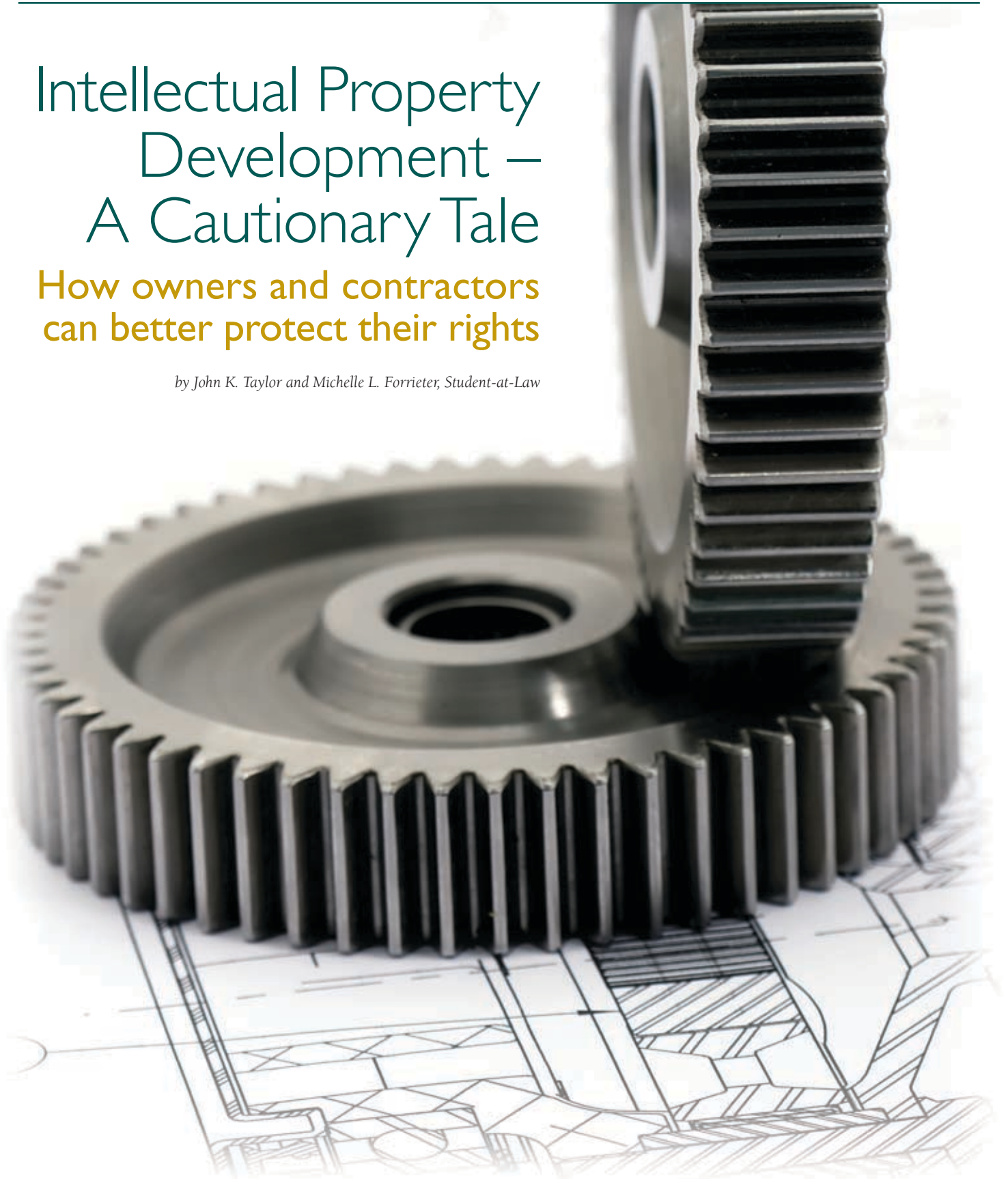
**FACT:** While storage costs for electronically stored information may be coming down, costs do remain, and it is not just the cost of storage. Large amounts of electronically stored information take more time to search and process, leading to wasted staff time and lost productivity. In addition, many records that could be legally destroyed, that have no further use, and that could be embarrassing or harmful if published, will still exist. Add to that the fact that privacy legislation requires that personal information be securely destroyed once there is no reasonable business or legal purpose for retaining it, so retaining personal information longer than necessary is illegal. Plan with your IT, Audit, Accounting, Human Resources and Legal groups for what you will keep and what will be destroyed.

If you are involved in claims management, procurement, the development of engineering documents, audit or IT, then you should consider whether you have been conducting your activities on the basis of these myths or if you have developed policies and procedures to comply with applicable legislation and legal interpretation. Organizing a company's policies, procedures and records can save you time, expense and inconvenience in (a) locating records to defend a claim and (b) determining if you have a proper basis to make a claim of your own. Avoiding the issue may leave you unable to respond to or negotiate your way out of your problems.

# Intellectual Property Development – A Cautionary Tale

**How owners and contractors  
can better protect their rights**

*by John K. Taylor and Michelle L. Forrieter, Student-at-Law*



## INTRODUCTION

**A** review of a Statement of Claim issued out of the Court of Queen's Bench in Alberta in June of 2007, leads one to reflect upon the fact that a clear, written contract can save a lot of grief. While the facts alleged in the initial Statement of Claim and the subsequent Statement of Defence are allegations only at this stage, there are lessons to be learned even from the allegations.

The story of the dealings between Suncor Energy Inc. ("Suncor") and MMD Design and Consultancy Limited/MMD Mineral Sizing (Canada) Inc. ("MMD") shows how uncertainty between parties about each other's rights can pave the way for a downward spiral in the relationship that leads all the way to the courthouse. These two companies began their relationship with MMD designing equipment for Suncor, but they have now ended up on opposite sides of a lawsuit, with real risk to their intellectual property. Could all of this have been avoided with a clear, written contract? There is, of course, no guarantee, but we can certainly say that this type of problem would be much less likely to occur as the contract would serve as a statement of the legal rights and obligations of the parties. Further, the very exercise of drafting the agreement requires the parties to focus at an early stage on any misunderstandings between them.

## BASIC FACTS AS ALLEGED IN THE STATEMENT OF CLAIM AND STATEMENT OF DEFENCE

According to Suncor, Suncor and MMD started out in a business relationship in April of 2003 which involved MMD designing and constructing some equipment for Suncor to help convert mined oilsands ore into a slurry, as part of Suncor's "At Face Slurry Technology". Suncor further suggests that MMD designed and built this equipment, and Suncor and MMD carried out its testing and implementation together.

During this testing process, however, Suncor alleges that it decided to develop its own smaller, lighter alternative to MMD's design. Suncor's design was developed to replace MMD's equipment, and, according to the statement of claim, MMD employees knew this. Suncor continued to have meetings with MMD throughout the development of its new machinery, allegedly sharing information about its design and construction

with MMD, information that Suncor claims was confidential and part of Suncor's trade secrets. It is suggested that MMD employees had physical access to the fully constructed and operational prototype of Suncor's new machinery. Suncor alleges that MMD used Suncor's confidential information to develop its own machinery, for which MMD filed a patent application.

MMD's main response to these allegations is that it had been developing technology related to the conversion of ore into slurry, and slurry transport, since as early as 2001, before its relationship with Suncor with respect to "At Face Slurry Technology" developed. MMD's claims that the technology developed by MMD was developed by it independently, and is fundamentally different from Suncor's technology. Additionally MMD states that Suncor never made it clear or took steps to suggest that it considered its technological information confidential. According to MMD, Suncor freely shared information about its technology with MMD and others in the industry without requiring MMD to sign a confidentiality agreement, and without objecting when MMD refused to sign a non-disclosure agreement in 2004.

Suncor did make one proactive attempt to protect its intellectual property rights, by filing a patent application for its new design on July 30, 2004. Beyond that application, however it relied on an alleged understanding between itself and MMD. Suncor claims MMD understood that all information about Suncor technology was confidential and that these were trade secrets owned by Suncor. MMD does not appear to have shared that understanding, and alleges that, based on a May, 2003 agreement, only MMD's own technology was to be protected by confidentiality requirements.

It appears that MMD filed patent applications internationally in January and March of 2004, while it was still working with Suncor, and before Suncor had filed its Canadian application. MMD then brought its international application to the Canadian level under the Patent Cooperation Treaty in January 2005, and applied under the Patent Act to have its January 2005 Canadian application given priority over Suncor's earlier application on the basis of MMD's prior international filings. Suncor claims that the subject matter of MMD's patent applications was derived, without authorisation, from Suncor's confidential technology.

## WHERE DO THEY GO FROM HERE?

The way things stand now, both sides may have a lot to lose, and are facing the ongoing expense and frustration of litigation unless they can somehow resolve this dispute. Each company has pending patent applications that will likely be challenged and delayed by the other, both in the patent office and in the courts. At least one of the parties, if not both, has hard work and ingenuity put into a design that may now be lost. If either party loses at the patent application stage then it could be sued by the other for patent infringement if it tries to use the technology it designed by itself, for itself.

Compounding the problems in this situation, is the fact that because the dispute is over intellectual property, the parties have to fight their battles on two fronts: at the patent application stage as well in the courts.

## PREVENTION OF THE PROBLEM

So what could either side have done to prevent all of these problems? Suncor's best bet to protect itself would have been to establish a clear agreement in writing, setting out all of the information Suncor wanted to protect, and having MMD openly acknowledge that all of that information was confidential and belonged to Suncor. If the relationship changed over time, the agreement should have been amended accordingly. Even if one party did try to claim the technology as its own, the true inventor could point to the agreement as evidence of ownership.

There are two main lessons to be learned from all of this. The first is that simply relying on oral communications or understandings between parties to protect interests as important as intellectual property rights is a risky proposition. Dishonesty aside, all it takes is for each side to have a different perception of what the understanding is, and the whole relationship can go sideways. The second is that even filing a patent application is not always sufficient to protect one's inventions, because these applications can be challenged, and sometimes even pre-empted. The bottom line: when it comes to something as important protecting one's own designs and technology, get it in writing.



# The Change Order

(Or “I Thought We Had A Deal  
Why Am I Paying For Extras?”)

**I**n our last couple of issues of *From the Ground Up* Construction Newsletter we have printed excerpts from the paper “*The EPC Contract and the Energy Lawyer*” written by John K. Taylor and Arnie Olyan. This is a further excerpt and the full article remains available upon request.

Unlike many contracts, an EPC Contract<sup>1</sup> typically provides a mechanism by which the parties actually contemplate amending the provisions of the contract from time to time. Utilization of these provisions, known as “change orders,” may be frequent or relatively infrequent, depending on the nature of the contract, the degree of specificity of the work initially described in the EPC Contract, the basis for the contract price, and other factors. In any event, change orders can significantly change both the cost and schedule of projects so they should be anticipated and accounted for in the EPC Contract and the reporting systems prescribed.

Consideration must first be given to who may propose a change order. An owner usually retains the right to modify (by addition, deletion, or substitution) the scope of work, the contract schedule, or any other part of the contract. The contractor will then evaluate the cost of the

modification and it will be for the owner to then decide whether to proceed to issue a change order, typically on the terms of the proposed modification and evaluation.

The circumstances under which a contractor may initiate a change order are typically more onerous. The owner will view such requests with some suspicion. In the majority of circumstances, the owner may suspect that it is being asked to pay “extra” for work that was already understood to be included in the EPC Contract. To minimize both the number and frequency of change orders, the EPC Contract will often provide that there must be an “event change” before application can be made or brought for a change order. While the definition of an event change may be the subject of some negotiation, it will typically be incumbent on the contractor to show an event (or events) has occurred giving rise to a material increase in the obligations of the contractor under the scope of work. Alternatively, a contractor may have to demonstrate that an event has had an adverse effect on the ability of the contractor to meet the project schedule. In either circumstance, the event: (a) must have occurred due to acts or omissions beyond the contractor’s control; (b) could not have been reasonably foreseen by an experienced contractor;

or (c) was not otherwise contemplated under the EPC Contract. All of these qualifications, and others, are used to limit the contractor's opportunity to obtain a change order.

Change orders are also common under longer running EPC Contracts to account for any changes in law coming into effect during the term of the contract.

In all cases, an evaluation of the change would be prepared by the contractor prior to the owner approving the request. Upon settlement of the change order, the EPC Contract price would typically be amended and change orders will cause corresponding adjustments to contract schedule, the contractor's work force plan, and other elements of the EPC Contract as applicable.

If parties are unable to reach agreements on adjustments necessitated by a change order, the owner will usually insist that the contractor proceed with the work and that the owner will establish adjustments (including the amount of compensation and any adjustments to the contract schedule). If all commercial efforts fail to provide agreement on the terms of the change order, the dispute may be resolved under the dispute resolution mechanism of the EPC Contract.

In some instances, utilization of the change order mechanism can be among the most contentious provisions of an EPC Contract. Under a lump sum contract, the change order is the instrument most commonly used by the contractor to press for price increases regarding: (i) any portion of the scope of work that the contractor or the owner misunderstood; or (ii) any costs that have been miscalculated. Conversely, the use of change orders may be discouraging to one or both parties if the reason for the change, and the corresponding delays or cost impacts, are the result of poorly drafted scope of work documents or an unworkable change order procedure. Perhaps the

change order mechanism is best understood when a contractor is retained very early in the initiative, the development of the scope is more iterative, and both parties are expecting change orders in the normal course as the project develops, changes, and changes again.

Without a solid understanding of the change order provision and the circumstances in which it is to be followed, parties may: (i) put themselves through needless stress in coming up with a fair and equitable method of agreeing upon bona fide changes; or (ii) be exposed to risk, by skewing their agreement through a subsequent, non-compliant course of conduct. Indeed, it is common for parties to ignore the change order provisions of an EPC Contract in favour of an alternative arrangement that becomes so imbedded that it becomes unreasonable to impose the express change order process on the parties. The western Canadian cases of *Kei-Ron Holdings Ltd. v. Coquihalla Motor Inn Ltd.*<sup>2</sup> and *Banister Pipeline Construction Co. v. TransCanada Pipelines Ltd.*<sup>3</sup> are perhaps two of the clearest examples of where the parties were well aware of the requirement for written change orders, yet chose to ignore these requirements. When the parties proceeded with changes based on verbal requests, they were forced to confront the uncertainty surrounding liability for the costs of performing extra work. It is at least arguable that this uncertainty would have been avoided if the parties had simply followed the change order provisions contained in the contract negotiated between them.

#### Footnotes

<sup>1</sup> For this article, "EPC contract(s)" collectively includes design-build, engineering, equipment purchase, construction management, pure construction, EPC and various forms of design-build-operate agreements.

<sup>2</sup> (1996), 29 C.L.R. (2d) 9 (B.C.S.C.)

<sup>3</sup> 2003 ABQB 599

# Drug Testing Revisited

by Rachel West

## INTRODUCTION

Pre-employment and on-the-job drug testing has been a hot topic in Canada for several years. Our April 2007 issue of *From the Ground Up* featured the article *Drugs & Alcohol – An Employer's Nightmare*. At the heart of the issue is the tension between an employer's responsibility to maintain a safe work-site and the individual employee's rights to privacy, freedom from interference and protection from discrimination. Over the last 15 years Canadian courts have tried to strike a balance between these competing

interests. The resulting disputes have been frustrating for employers because courts have allowed testing in only the most restrictive circumstances.

## THE LEADING CASE UP TO NOW

Until recently and at the time of our last article, the Ontario Court of Appeal's decision in *Entrop v. Imperial Oil Ltd.*<sup>1</sup> ("Entrop") has been the leading case on employment drug and alcohol testing in Canada for the last 13 years. The Court of Appeal in

Entrop determined that pre-employment drug testing for safety sensitive positions is discriminatory, because (unlike alcohol testing) it does not indicate current or future impairment on the job. Specifically, the Court of Appeal asserted that drug testing only indicates *prior drug use*. Thus, pre-employment drug testing is only useful for the identification of individuals who *have used drugs previously* (in some cases days before the test), which makes such testing discriminatory in nature and not reasonably necessary to ensure workplace safety.



**However, a recent Alberta Court of Appeal decision may be one of the first decisions to tip the scales towards a more pragmatic approach to drug testing on safety-sensitive worksites.**

Canadian courts of all levels have followed *Entrop's* restrictive approach to drug testing. Provincial human rights commissions have also followed *Entrop's* lead and found drug testing to be discriminatory in all but the most restrictive situations.

### ALBERTA COURT OF APPEAL HAS A DIFFERENT VIEW

However, a recent Alberta Court of Appeal decision may be one of the first decisions to tip the scales towards a more pragmatic approach to drug testing on safety-sensitive worksites. The long-awaited decision in *Alberta (Human Rights and Citizenship Commission) v. Kellogg Brown & Root Co.*<sup>2</sup>, known as the “*Chiasson*” decision, may assist employers who want to perform pre-employment and on-the-job drug testing in the interest of workplace safety.

John Chiasson (“*Chiasson*”) was offered a position with Kellogg, Brown & Root (“*KBR*”), a construction company. As a precondition to

employment, Chiasson was required to pass a drug test. Chiasson took the pre-employment drug test and immediately started work. Nine days after Chiasson began working for KBR, his drug test came back positive. When questioned, Chiasson admitted to using marijuana five days before the test. KBR terminated Chiasson's employment immediately.

Chiasson filed a complaint with the Alberta Human Rights and Citizenship Commission. At the hearing, Chiasson admitted that he was a recreational marijuana user, but asserted that he was *not* addicted to it. The Human Rights Panel found that KBR's drug testing policy was discriminatory with respect to addicted persons. However, since Chiasson asserted that he was not an addict, he was not discriminated against based on a real or perceived disability.

In 2006 the Alberta Court of Queen's Bench<sup>3</sup> reviewed the Panel's decision, and found that Chiasson was discriminated against based

on *perceived* disability. Despite his admission that he was not addicted, the Court held that Chiasson was discriminated against because KBR's policy treated anyone who tested positive as if they were addicted, and thus disabled. Moreover, the Court found that KBR's policy went further than necessary to meet its workplace safety objectives, and failed to accommodate those with real or perceived disabilities. KBR was ordered to revise their policy. Not surprisingly, this decision was met with some confusion, as it was unclear how an individual who asserted he was not an addict (and thus not disabled) could be granted protection under the Alberta Human Rights, Citizenship and Multiculturalism Act.

The Alberta Court of Appeal has now disagreed with the lower Court. In a unanimous decision, the Court of Appeal found a rational connection between KBR's policy and its workplace safety objective. The Court of Appeal asserted that KBR's policy was directed at the *actual effects* of marijuana use of all kinds (recreational and addict), and not the perceived effects suffered by marijuana addicts. In direct opposition to the decision in *Entrop*, the Court of Appeal stated:

[T]he effects of casual cannabis use sometimes linger for several days after its use. Some of the lingering effects raise concerns regarding the user's ability to function in a safety challenged environment...The purpose of the policy is to reduce workplace accidents by prohibiting workplace impairment.

### CONCLUSION

The *Chiasson* decision has significance for employers who wish to enforce pre-employment and on-the-job drug testing policies. The shift towards a pragmatic approach may mean that, with careful policy drafting and implementation, employers may be better able to meet their workplace safety objectives without the risk of attracting a human rights complaint.

### Footnotes

<sup>1</sup> [200] O.J. No. 2689 (C.A.)

<sup>2</sup> 2007 ABCA 426

<sup>3</sup> 2006 ABQB 302



# BD&P's Construction Team

**B**D&P's Construction Team is comprised of a team of litigators and solicitors who offer full service representation in all facets of the construction industry.

Our Team represents owners, contractors, sub-contractors, engineering firms, developers, banks, and other financial institutions on a wide-range of construction issues ranging from the straight forward to the complex. We review, negotiate and prepare terms and conditions and other documentation for varied construction and engineering projects; provide practical, timely and expert legal support throughout the construction process; and provide experienced litigation services when required.

BD&P's Construction Team represents a diverse range of client interests from those of small local contractors to developers of large-scale energy and infrastructure projects. Whether our clients require the review of a contract, the arbitration of a construction dispute, or the coordination and preparation of the multi-faceted and complex series of transactions demanded by a major project, BD&P is able to provide the individual lawyer or assemble a team with the appropriate depth and experience.

For your easy reference, we highlight both our Significant Areas of Service and examples of Major Projects in which either individual firm lawyers or the firm were involved, which include some of the largest projects carried out in Canada.

#### Significant Areas of Service:

- ◆ Negotiation and preparation of tender packages and joint venture, confidentiality, consulting, engineering services, and architectural services agreements
- ◆ Negotiation and preparation of construction, construction management, sub-contract, supply and mining services agreements
- ◆ Negotiation and preparation of Engineering, Procurement, & Construction (EPC) and design/build contracts
- ◆ Negotiation and preparation of Engineering, Procurement, & Construction Management (EPCM) contracts
- ◆ Delay claims
- ◆ Industrial design disputes

- ◆ Construction and contract disputes
- ◆ Tender disputes
- ◆ Engineering claims
- ◆ Lien claims
- ◆ Insurance issues including liability, builder's risk, errors and omissions, and professional liability coverage
- ◆ Regulatory and municipal planning approvals
- ◆ Preparation of construction security documentation
- ◆ Representation at arbitrations and mediations
- ◆ Service as arbitrators and mediators in construction disputes

#### MAJOR PROJECT EXPERIENCE:

- ◆ **Hibernia Project** – offshore oil production platform off coast of Newfoundland
- ◆ **Terra Nova Project** – floating production, storage & offloading facility in oilfields on Grand Banks
- ◆ **Sable Island Project** – offshore natural gas recovery project off coast of Nova Scotia
- ◆ **Horizon Oil Sands Project** – oil sands project in northern Alberta
- ◆ **Muskeg River Oil Sands Project** – oil sands project in the Athabasca oil sands region of northern Alberta
- ◆ **Long Lake Oils Sands Project** – development project of heavy oil infrastructure in the Athabasca oil sands region of northern Alberta
- ◆ **Tanguh Project** – a liquefied natural gas project in Indonesia
- ◆ **Confederation Bridge Project** – fixed link bridge across Northumberland Strait
- ◆ **Sakhalin Island Project** – large scale oil and gas development project on Sakhalin Island in Russia
- ◆ **Husky Oil Upgrader** – development of Lloydminster Heavy Oil Upgrader
- ◆ **MEGlobal** – worldwide joint venture for manufacture and sale of ethylene glycols

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