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IS YOUR MASTER SERVICES AGREEMENT A PREVENIENT ARRANGEMENT UNDER THE ALBERTA *BUILDERS' LIEN ACT*?

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It makes sense that businesses would like to develop long term relationships with preferred contractors and suppliers, but do master service agreements and other long term arrangements have an effect on the parties rights and obligations under the *Builders' Lien Act*? The answer is that if an arrangement is a *prevenient arrangement* then:

- the party contracting for the work or service (an owner, general contractor or anyone else) will have a significantly increased exposure for holdback; and
- the party performing the work or providing the service or goods (typically the designer, contractor or supplier or their subcontractors) should not be paid out the holdback until the end of the whole arrangement – which can seriously and negatively affect cash flow.

The *Builders' Lien Act* bases the rights and obligations of the various parties on the contracts between them. This means, for example, that each contract will have its own lien fund for lien claimants. The common law has developed the concept of a prevenient arrangement. A prevenient arrangement arises where a single contract is deemed to cover a series of transactions. This means that the holdback amounts accumulate for the whole prevenient agreement and the period for filing a lien in relation to the first transaction is extended to the end of the applicable statutory period after the last transaction.

A prevenient arrangement was described in ***Blue Range Resource Corp. (Re)***[1] by Justice Romaine as follows:

> A prevenient arrangement is said to exist where there is a preliminary understanding between parties that they are entering into an ongoing relationship. This preliminary understanding does not have to be a binding contract or contain all the terms upon which materials or services are to be supplied, but it serves to link together what would otherwise appear to be a series of contracts into one continuing contract or open account ...[2]

It is a question of fact as to whether or not the services or work performed have been provided under separate or linked transactions.[3] Justice Romaine further stated that:

> [T]he scope and extent of the work to be done further to the preliminary understanding must be determinable with a sufficient degree of certainty to constitute the "thread" that serves to link the subsequent supply of goods or services together.[4]

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1 *Blue Range Resource Corp (Re)* (1999), 254 A.R. 103 (Q.B.)
2 *Blue Range Resource Corp (Re)* (1999), 254 A.R. 103 (Q.B.) at page 105
3 For a recent case in which a prevenient arrangement was found, see *Consun Contracting Ltd. v. Surmont Sand & Gravel Ltd.*, 2006 ABQB 164
4 *Blue Range Resource Corp (Re)* (1999), 254 A.R. 103 (Q.B.) at page 106

In his judgment in ***Schlumberger Holdings (Bermuda) Ltd. v. Merit Energy Ltd.***[5] , Lovecchio J. determined that the burden of proof lies with the lien claimant and summarised the factors to be considered in establishing a prevenient arrangement as follows:

- a limited time frame
- a designated area of service
- a guarantee of specific amount of work or sales
- exclusivity between the parties or advance discussions of specific requirements[6]

Many owners and contractors negotiate master contracts or umbrella agreements to manage their relationships. These are over-arching agreements, the purpose of which is to establish a long-term business arrangements between the parties and to set out the terms and conditions that will apply to each transaction between the parties. Once a master contract or an umbrella agreement is negotiated, the owner can issue work orders, releases or authorizations to initiate the performance of specified work without renegotiating the terms and conditions each time.

If a master contract or an umbrella agreement exists, it opens the door to litigation from lien claimants arguing that a prevenient arrangement exists. While not a panacea, language such as the following may assist in establishing that a prevenient arrangement does not exist:

> The parties agree that each Work Order will be an independent and separate contract from all other Work Orders, for all purposes, including, but not limited to, the application of the applicable lien legislation. In addition, this Master Contract does not create, nor will be deemed to create a prevenient arrangement or general contract between the Owner and the Contractor. The purpose of this Master Contract is to agree to certain terms that will govern the relationship between the Owner and the Contractor. However, each Work Order will set out the specific terms and conditions relating to the Work and will be a separate contract in relation to the law, including, but not limited to, the applicable lien legislation.

If a prevenient arrangement is found to exist, then it is worthwhile knowing the consequences of the arrangement from a *Builders' Lien Act* point of view. The holdback is typically paid out to the contractor 45 or 90 days[7] after the completion of the project. Where, for example, there are three projects that the contractor works on, there could be the following payments made:

Project 1 Completion March 1, 2009		Project 2 Completion June 1, 2009		Project 3 Completion September 1, 2009	
Contract Price	Holdback Paid on April 16, 2009	Contract Price	Holdback Paid on July 17, 2009	Contract Price	Holdback to be Paid on October 17, 2009
$900,000	$90,000	$2,000,000	$200,000	$130,000	$13,000

5 Paraphrased from Schlumberger Holdings *(Bermuda) Ltd. v. Merit Energy Ltd.* 2001 ABQB 34

6 *Schlumberger Holdings (Bermuda)* Ltd. v. Merit Energy Ltd. 2001 ABQB 34, at para. 39

7 In 2001, an amendment to the *BLA* increased the period for filing a lien against an "oil and gas well" or "oil and gas well site" to 90 days, although these terms are not defined.

If the contractor becomes insolvent on October 1, 2009, then, if these projects are considered to be separate contracts, the holdback has been paid out on the first two projects and there are no issues with respect to those holdbacks. In relation to the third project, the owner has a $13,000 holdback and that holdback, plus any amount owing under the contract, will form the lien fund and the lien claimants are entitled to the lien fund on a *pro rata* basis. The owner's liability is capped at the amount of the lien fund.[i]

If, however, a prevenient arrangement is established, then all of the work would be deemed to be under one contract and the holdback would be the sum of $90,000 + $200,000 + $13,000, for a total of $303,000. This would be the exposure of the owner to the lien claimants, plus the amount unpaid under any contract, notwithstanding that $290,000 of the $303,000 has already been paid out to the insolvent contractor.

When entering into long term relationships, contracting parties should be aware of the effect of the *Builders' Lien Act* on their arrangements and, where possible, should be proactively making their intent regarding those relations known before the contract is tested.

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[i] See section 25 of the *Builders' Lien Act*:

Liability of owner

25 An owner is not liable under this Act for more than

(a) the total of the major lien fund and the minor lien fund, or

(b) the major lien fund, where a minor lien fund does not arise under section 23.