

September 2009

## SETOFF DEFENCE

We have discussed set-off on a number of occasions: in the context of a general who sets off against a sub when there are no subs claiming (see May 2006 newsletter); in a trust action (see January 2000 newsletter); and as a defence to set off debt on one project against a claim on another (see November 1998 newsletter). In none of these newsletters did we discuss the rules for setoff. We wish to remedy that omission in the context of D.J. Venasse Construction Ltd. v. MVD Properties Inc., a 2009 decision of the Ontario Divisional Court.

### Can't Pay

An owner owed its general \$2.1 million out of a total contract price of \$3.1 million. We do not understand why the general would have continued its work given the huge amount owing on contract. Not surprisingly, the general's subs had registered claims for lien.

The general commenced an action for payment, but never liened. The general and owner then entered into an agreement by which the owner agreed to pay \$500,000 and then subsequent periodic payments. The agreement specified that if the owner defaulted, it would have 14 days to file its statement of defence to the general's action.

The owner made the first payment of \$500,000 and the general used it, along with its own funds, to pay all of its subs and discharge their liens. The owner then defaulted.

The general and owner entered into a second agreement. The owner was to pay the balance owing in monthly payments of \$200,000. The owner made two payments and defaulted again.

The owner then delivered its statement of defence. It acknowledged that, had the general completed its work without deficiencies, the owner would have owed the general \$1.2 million. However, the owner claimed it did not owe the general anything because of defects and deficiencies in the general's work. It claimed setoff as a defence and brought a counterclaim for the damages that it claimed.

The general brought a motion for summary judgment, arguing that the parties had settled the outstanding amount and that the defence was a sham.

### Motions Judge

The motions judge noted that the parties agreed that the amount outstanding on the contract was \$1.2 million and decided that, in the agreements, the owner had admitted liability. He held that the deficiency claims were independent claims that the owner could not set off, but could prosecute

by way of its counterclaim. The judge was particularly disturbed that the owner had not raised the alleged deficiencies in any of its prior negotiations.

The motions judge therefore granted judgment for \$1.0 million and stayed enforcement on the remaining \$200,000 until the counterclaim was dealt with. The motions judge never stated how he arrived at the \$200,000 amount.

The owner appealed.

### Divisional Court

The Court disagreed with the findings of the motions judge in two key aspects:

1. There was no unequivocal admission of liability in the agreements. Why would the owner have the right to deliver its statement of defence if it had admitted liability? Further, as long as it could deliver a statement of defence, it could claim setoff, whether it had raised the issue in the negotiations or not.

2. In order for a defendant to claim legal setoff, there must be two debts. As the motions judge noted, the owner could not obtain legal setoff because it sought damages rather than payment of a debt. However, equitable setoff applies when there are mutual obligations arising out of the same contract, regardless whether the claims are in debt or in damages. When there is a close relationship between parties that gives rise to mutual claims, equity will not permit

one of those claims to be enforced without accounting for the other. A claim for deficiencies in the work of the general satisfies this test. It would be inequitable to allow a general to obtain judgment for the full amount of the work, if it did not complete that work or if the work that it did complete was deficient.

Accordingly, since the motions judge decided that there was a genuine issue for trial regarding the alleged deficiencies and since there can be no summary judgment as long as there is a genuine issue for trial, the entire matter had to be dealt with at trial. Accordingly, the Court allowed the appeal (with costs to the owner of \$20,000) and dismissed the general's summary judgment motion.

## Problems

We have some technical concerns with this decision. The motions judge held, without giving reasons, that \$200,000 was adequate to address the counterclaim. He did not provide any basis for his calculation. If he did not do so because the owner did not adduce evidence to show that the deficiencies would cost over \$1.2 million to remedy, then the court should have allowed judgment for \$1.2 million less the damages that were in issue. Were there really \$1.2 million in deficiencies? We rather doubt it.

Further, just because the motions judge did not calculate how he arrived at his figure of \$200,000 does not mean that the court could not have done so.

We wonder why the general would have entered into agreements with the owner for

the payment of monies due, if it allowed the owner the ability to default under the agreements with impunity.

We suppose the general figured that if the owner defaulted under the agreements, there would be no harm to the general. It would still get its \$500,000 and get rid of its subs and would be in no worse position than if it had made no deal at all.

However, we still cannot understand why the general would have put itself in the position in which it settled with, and paid out, its subs and still allowed the door to be open for the owner to claim that the subs performed their work improperly. Something must be missing - because what we see does not make sense.

You will find this and prior newsletters posted on our website.

**Speigel Nichols Fox LLP**  
30 Eglinton Ave. W., Suite 400  
Mississauga, Ontario L5R 3E7  
Tel: 905-366-9700  
Fax: 905-366-9707  
www.ontlaw.com

Jonathan Speigel\*+  
Brian Nichols  
Irving Fox  
Ian Latimer\*  
Robert McIntyre  
Susanne Balpataky\*  
Jeffrey Tighe\*  
Philip O'Shea  
Paul Roth\*

\* members of construction litigation group  
+ certified by Law Society as a specialist  
both in civil litigation & construction law  
+ roster mediator - Ontario Mandatory  
Mediation program - Toronto

## ANNOUNCE- MENT

Jeffrey Tighe has joined our litigation and construction department.

Jeff has a B.Sc. from Queen's University, an MBA from Wilfrid Laurier University, and a law degree from University of Manitoba. He was called to the Bar in Ontario in 1999. Since then, he has practised in commercial litigation and construction law.

In his spare time, of which there may be little, he is currently researching and writing a book in the field of military history.

## MISSION STATEMENT

**OUR CLIENTS COME  
FIRST. EVERYTHING  
ELSE FOLLOWS.**

*Building Relationships is provided as information to our clients and friends on new developments and legal issues of significance. The information is not intended to provide legal services. Readers should seek professional legal advice on any issues that directly concern them.*