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CONSTRUCTION CLAIMS AND INSOLVENCY

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SPEAKER

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Construction & Infrastructure

- Jessica's core practice involves the drafting and negotiation of major strategic and operational commercial and construction contracts.
- Building contracts including advising on standard JCT, NEC3 and NEC4, and Partnering and Alliancing contracts, bespoke construction contracts, professional appointments, collateral warranties; repairs and maintenance contracts.
- Development agreements; framework agreements; agreements for lease; construction related elements of funding agreements; drafting and reviewing parent company guarantees; advance payment and performance bonds.
- She has been a deputy director of the Quantity Surveyors Division of the RICS responsible for contracts; and also served on the JCT drafting committee.



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Agenda for today

CONSTRUCTION DISPUTES AND INSOLVENCY

- Contractual claims in construction disputes – the usual battlegrounds
- Routes to recovery
- Recent case law and judicial guidance
- Claims notes

Contracts and disputes

- The key is to identify:
 - the contract
 - the Parties
 - terms and conditions
 - enforcing the contract and security



Essential JCT construction contract speak

- Some key terms:
 - Construction Act
 - Contract Sum
 - Valuation
 - Interim Payment
 - Changes/Variations
 - Notices
 - Instructions
 - Relevant Events/Matters
 - Extension of time
 - Final Account
 - Retention
 - Performance bond/parent company guarantee
 - Practical Completion
 - Liquidated/ascertained damages
 - Termination
 - Insolvency



Construction disputes and insolvency

Summary of types of contractual claims in construction contracts

- Payment
- Delay claims (LADs / Extensions of time / Loss and expense)
- Quality and defects
- Default and termination

see end slides for more

Making contractual claims under construction contracts

- Check contractual provisions
- Construction contracts are notices driven - get your notices right



Construction Disputes and Insolvency

ROUTES TO RECOVERY

- Adjudication
 - A form of dispute resolution applicable to construction contracts as defined in the Construction Act.
 - An independent third party adjudicator makes a decision based on written submissions from the parties, often within 28 days. No entitlement to recover costs.

Construction Disputes and Insolvency

NOTICES, NOTICES, NOTICES AND “SMASH AND GRAB”

- HGCRA 1996 as amended (“Construction Act”) & Scheme
- The availability of the remedies based on the Construction Act is determined by a strict notices regime:
 - right to stage or interim payments + adequate mechanism for determining what payments become due & when;
 - final date for payment of any sum which becomes due;
 - provision for Payment Notices failing which the Act provides mechanism for determining “notified sum” based on Employer’s Payment Notice or Contractor’s application.

Construction Disputes and Insolvency

- Paying party may give a Pay Less Notice, absent which the ‘notified sum’ **must** be paid by final date for payment.
- “smash and grab” is a “quick win” claim by a Contractor pursued through an adjudication based on the Payer’s failure to serve the correct notices, and is often successful, irrespective of the true value of the works.



Construction Disputes and Insolvency

NOTICES AND “SMASH AND GRAB”

- Grove Developments Ltd v S&T (UK) Ltd
 - Design & build of new Premier Inn Hotel at Heathrow (JCT D&B 2011).
 - Adjudicator’s decision required for payment of application in the sum of £14m.
 - Payment Notice held to be out of time
 - Pay Less Notice held to be invalid
- Grove considered sum due to be £0.00.
- Grove commences Part 8 proceedings (seeking the court’s decision on a question which is” unlikely to involve a substantial dispute of fact”) for:
 - declaration of right to cross adjudicate;
 - determination of validity of
 - (i) Pay Less Notice; +
 - (ii) Notices for deduction of LADs.

Construction Disputes and Insolvency

NOTICES AND SMASH AND GRAB

Judgement

- An Employer *does* have the right to bring a second adjudication to establish the “true value”, after *paying* the notified sum.
- Under the Construction Act the adjudication provisions are subordinate to the payment provisions.
- The operation of the provisions of the Act relating to the interim application, payment notice and pay less notice do not provide a valuation of the works done.
- The provisions were for cash flow purposes, and it remained *open* to either party to challenge the correctness of the notified sum by adjudication.

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ROUTES TO RECOVERY

- Litigation
 - A formal court process. The parties must comply with various procedural steps (disclosure, witness statements, expert evidence) following which the trial takes place before a Judge. Can be a lengthy and expensive process (successful party normally recovers a significant proportion of its costs). Judgments are public.

Construction Disputes and Insolvency

ROUTES TO RECOVERY

- Arbitration
 - Similar to court proceedings in terms of procedure, timescale and costs, but takes place in front of a privately appointed (and paid) arbitrator. The proceedings are private.



Construction Disputes and Insolvency

ROUTES TO RECOVERY

- Alternative Dispute Resolution (ADR)
 - Various forms of ADR, such as expert determination; or mediation, where a third party assists the parties in reaching a resolution of the dispute.



Construction disputes and insolvency

- Cashflow insolvency and the introduction of adjudication for construction contracts
- Insolvency meaning and termination options under JCT Contracts



Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- **How does Insolvency and adjudication impact claims?**
- Adjudication is the main route to recovery for construction claims
- Michael J Lonsdale (Electrical) Limited v Bresco Electrical Services Limited (*in liquidation*) [2018] EWHC 2043 and EWCA [2019]
 - Construction contract (sub-sub-contract)
 - Bresco Electrical Services Ltd ('Bresco') agreed to perform electrical installation works for Michael J Lonsdale (Electrical) Ltd ('Lonsdale').
 - Contractual dispute
 - Mutual allegations of wrongful termination
 - Bresco left the Site
 - Bresco went into liquidation in March 2015 and its *liquidator* commenced an adjudication against Lonsdale over two years later.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- Lonsdale sought an **injunction** to prevent the continuation of Bresco's adjudication claim, which Fraser J **granted** in the TCC last year on the basis that:
 - (1) adjudicators did not have jurisdiction to deal with claims advanced by companies in insolvent liquidation; and
 - (2) the “*utility*” argument where Fraser J (quoting Edwards-Stuart J) said he was “*unable to see how it would be either just or convenient to permit an adjudication to continue in circumstances where the decision of the adjudicator will be incapable of enforcement*”.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- The Court of Appeal **upheld the injunction** stopping Bresco's claim:
 - Coulson LJ found, contrary to the judgment at first instance, an insolvent company's contractual claim did not cease to exist at liquidation: “...*technically the adjudicator would **have jurisdiction** to consider the claim advanced by a company in liquidation*”.
 - Coulson LJ did *not* accept that Bresco's *right* to refer a dispute to adjudication was **automatically lost** when they went into liquidation.
 - However he agreed that the injunction granted to restrain the continuation of the adjudication was the appropriate remedy in the circumstances.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- *On the facts*, there was nothing to demonstrate that it would be **just or convenient** for the underlying adjudication to continue.
- Bresco had been **insolvent for over three years** before the adjudication referral, there was no suggestion Bresco could ever trade again and Lonsdale's cross-claim had been issued by the time of the adjudication.
- There was **no good reason** to make Lonsdale incur the costs of defending a claim in adjudication that could not be enforced ie
 - The “utility” argument - the court held that since, where the responding party has a cross claim, an adjudicator's decision in favour of a company in liquidation would not normally be enforced, continuing with the adjudication was “an exercise in futility”.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- Court of Appeal **upheld the injunction** to stop Bresco's adjudication.
- Coulson LJ considered that adjudication and the Insolvency Rules regime were not compatible:
 - There was a basic incompatibility between adjudication and the insolvency regime.
 - The former was a method of obtaining an improved cashflow quickly and cheaply, but was likely to result in injustice. The latter involved the taking of a detailed account as between the company and creditor, and the careful calculation of a net balance one way or the other, or quantifying the company's net claim against a creditor.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- The incompatibility could be seen in the different processes that each regime entailed, in a comparison of the results that might be available, and in a consideration of the wider issues that could arise if companies in insolvent liquidation regularly sought to refer claims to adjudication.
- It would only be in exceptional circumstances that a company in insolvent liquidation (*and* facing a cross-claim) could refer a claim to adjudication, succeed in that adjudication, obtain summary judgment and avoid a stay of execution.
- Thus, in the ordinary case, even though the adjudicator might technically have the necessary jurisdiction, it was not a jurisdiction which could lead to a meaningful result.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- Meadowside Building Developments Ltd (in liquidation) (**Meadowside**) v 12-18 Hill Street Management Company Ltd (**HSMC**) (High Court judgment given 10 October 2019).
 - In 2015, **Meadowside** was placed into **voluntary winding up**. Under the parties' JCT Minor Works Building Contract, this required a final account to be taken of the sums due between the parties.
 - Equally, under Rule 4.90 of the Insolvency Rules 1986 (now Rule 14.25) an account had to be taken of all the parties' claims and cross-claims.
 - Meadowside considered there to be sums owed to it from HSMC,
 - HSMC considered that it was a **creditor** in Meadowside's insolvency.
 - By 2017, efforts taken by Meadowside's Liquidators to realise a sum from HSMC had *not* been successful. The liquidators engaged Pythagoras Capital Limited ('Pythagoras') to take over the claim

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- In 2018, Meadowside referred its claim against HSMC to adjudication.
- It was represented by Pythagoras in the adjudication proceedings.
- HSMC did not participate in the adjudication on grounds that the adjudicator lacked *jurisdiction* as a result of Meadowside's insolvency (see *Bresco*).

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- On 3 April 2018, the adjudicator produced a decision in which a net balance *to* Meadowside of £32,629.63 was found to be due.
- On 31 July 2018 and before enforcement proceedings were commenced against HSMC, the high court judgment in *Bresco v Lonsdale* was handed down; although on 24 January 2019, the Court of Appeal overturned Fraser J's decision on jurisdiction (ie the adjudicator did not lack jurisdiction)

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- Court had to determine the effect of the Court of Appeal's decision in *Bresco*, in particular what was meant by the “exceptional circumstances” in which an **insolvent company** may properly **adjudicate** on a dispute *and* enforce any award in its favour.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- Court in *Meadowside* recognised *potential exceptions* to the Bresco position, for example where:
 - the adjudication dealt with all the parties' mutual claims (ie opposite to a smash and grab);
 - there is a satisfactory guarantee in relation to any sum awarded, and/or where the sum is temporarily ringfenced.
- On the facts, the court did *not* grant summary judgment to enforce the award, but highlighted possible exceptions to the Bresco rule.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

What about **Company Voluntary Arrangements**?

- Cannon Corporate Limited (Cannon) v Primus Build Limited (Primus) [2019] EWCA Civ 27 .
 - **Court of Appeal** *enforced* Adjudicator's decision despite Referring Party being in a **CVA**.
 - Court dismissed the appeal noting "Although each case will turn on its own facts, there are potentially important differences between a company in liquidation and a company in a CVA".
....
 - The factual background to the Cannon appeal concerns a Creditors Voluntary Arrangement.
 - Cannon engaged Primus to design and build a new hotel.
 - Primus served a payment notice, and Cannon served a pay less notice in response, putting the amount due at nil.
 - Cannon then served a notice of termination on Primus. There followed a number of adjudications and litigation between Primus and Cannon
 - In July 2017, Primus entered into a CVA.
 - The CVA had been accepted as, although the company was insolvent, there was a clear way forward that would result in all creditors being paid in full, and Primus continuing to trade. This was a key distinction with the insolvent liquidation in Bresco.

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- In March 2018 Primus was awarded in excess of £2.1 million following a 4th adjudication for damages for repudiatory breach of contract.
- The adjudicator considered, and almost entirely rejected, Cannon's cross-claims in reaching the decision.
 - Primus commenced enforcement proceedings.
 - Cannon accepted judgment may be entered but sought a stay of enforcement.
 - HHJ Waksman QC declined to grant the stay because the financial position of Primus had arisen partly due to Cannon's refusal to pay the monies awarded to Primus.
 - A stay of execution was refused
 - The Cannon appeal settled before it could be heard and so the CA decided that no further order would be made in the Cannon appeal

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

Court stated :

“[A CVA] is designed to try and allow the company to trade its way out of trouble. In these circumstances, the quick and cost-neutral mechanism of adjudication may be an extremely useful tool to permit the CVA to work...courts should be wary of reaching any conclusions which prevent the company from endeavouring to use adjudication to trade out of its difficulties.”

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

BUT

- **Indigo Projects London Ltd v Raizin & Or [2019] [EWHC].**
 - Claimant, Indigo had a successful adjudication award based on Raizin's failure to serve pay less notice.
 - After issuing proceedings to **enforce** the *award* by way of summary judgement **Indigo** entered into a **CVA**.
 - Raizin resisted and sought a **stay of execution** on the basis that its counter-claims had not yet been determined so paying the adjudicator's award would result in the CVA supervisors distributing that sum amongst the general body of creditors and would not be available to offset any *cross-claim* by Raizin

Construction Disputes and Insolvency

SOME RECENT CASE LAW AND JUDICIAL GUIDANCE

- **Held** that it would *not* be just to *enforce* the adjudicator's decision so that the award would be paid *after* the company had entered into a CVA.
 - It would not be taken into account as part of the exercise of assessing the balance of dealings between the parties, as it would have done had it been paid *before* the CVA.
 - Judge held it would be *wrong* in principle to *enforce* the decision and would *distort* the process of accounting between the parties.
- It was relevant that the adjudicator's decision was not on the merits of one party's case and did *not* deal with all matters between the Parties (arguably the case in *Primus*); nor was it a true valuation of the work - rather it was a "smash and grab" (see above) based solely on failure to serve a pay less notice.

Construction Disputes and Insolvency

CLAIMS NOTES



Construction Disputes and Insolvency

LOSS AND EXPENSE

What is loss and expense?

- Additional costs incurred as a result of delay or disruption to the progress of the works, caused either by matters within the employer's control or breaches of contract by the employer. Costs may be incurred as a result of:
 - delay to the works
 - disruption to the works
- Categories of loss and expense include:
 - Increased preliminaries
 - Overheads
 - Wasted management time
 - Loss of productivity / inefficient working

Construction Disputes and Insolvency

LOSS AND EXPENSE

- Contractual provisions normally include entitlement to loss and expense and mechanism for claiming.
- Check and follow notice requirements.
- Contractor needs to show delaying event and associated financial effects.
- Can be difficult where there are numerous events.
- There may be multiple causes of loss and expense - better if you can link each loss caused to a particular event of disruption or delay.
- Records, records, records!

Construction Disputes and Insolvency

LOSS AND EXPENSE

- If Contractor cannot separate individual causes and consequences of events to establish loss, consider global claims
- Society of Construction Law Delay and Disruption Protocol:
 - *“A global claim is one in which the contractor seeks compensation for a group of Employer Risk Events but does not or cannot demonstrate a direct link between the loss incurred and the individual Employer Risk Events.”*
- Global claims are discouraged by the protocol
- If it is shown that any material part of the global loss is not due to an Employer Risk Event, and it is not possible for the assessor to assess that value of that part, the entire claim *may* fail

Construction Disputes and Insolvency

LOSS AND EXPENSE

- Walter Lilly & Co v (i) Mackay and (ii) DMW Developments [2012]
- Mr Justice Akenhead

“the Contractor has to demonstrate on a balance of probabilities that, first, events occurred which entitle it to loss and expense, secondly, that those events caused delay and/or disruption and thirdly that such delay or disruption caused it to incur loss and/or expense”

“There is nothing in principle “wrong” with a “total” or “global” cost claim. However, there are added evidential difficulties ...

“The fact that one or a series of events or factors (unpleaded or which are not the risk or fault of the claimant contractor) caused or contributed ... to the global loss does not necessarily mean that the claimant contractor can recover nothing.”

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

- LADs are applicable in the event of certain specified breaches of contract by the Contractor, generally where the contractor fails to achieve practical completion by the completion date
- LADs, as opposed to general damages, do not require the claimant to prove that the losses claimed have actually been suffered
- Avoids the expense and difficulty of having to prove the actual damage suffered as a result of the breach.
- The rate of liquidated damages must not be ‘unconscionable’ or ‘extravagant’
- The test used to be whether the LADs were a genuine pre estimate of loss.

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

Following the cases of *Cavendish Square v Makdessi* or *Parking Eye v Beavis* the test now is:

“Whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation.”

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

- Contractual procedure for claiming liquidated damages
- Procedure generally governed by the provisions in the contract
- JCT Design & Build 2016
- Clauses 2.28 and 2.29 – provide that before liquidated damages can be deducted the Employer is required to give 3 separate notices in sequence.
- The 3 notices required are:
 - i. Non-Completion Notice
 - ii. Warning Notice cl 2.29.1.2
 - iii. Notice Requiring payment cl 2.29.2
- Potentially a fourth notice – Pay Less Notice

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

Non-Completion Notice

- Clause 2.28
- If the Contractor fails to complete the Works or a Section by the relevant Completion Date, the Employer shall issue a Non-Completion Notice.

Warning Notice

- Clause 2.29.1.2
- The Employer is required to serve a notice stating that it “may” require payment of or “may” withhold or deduct liquidated damages.
- The Warning Notice must be given before the due date for the final payment

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

Notice Requiring Payment

- Clause 2.29.2
- Notice that the Employer requires the Contractor to (i) pay liquidated damages and/or (ii) that the Employer will withhold or deduct liquidated damages at the rate stated in the Contract.
- The Notice Requiring Payment must be given not later than 5 days before the final date for payment for the final payment and can only be sent after the Non-Completion Notice or the Warning Notice.

A Fourth Notice?

- Pay Less Notice
- If the Notice Requiring Payment is based on (ii) above, i.e. that the Employer will withhold, then the Employer must also serve a Pay Less Notice.
- Also 5 days before the FDP for the final payment.

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

- What happens to liquidated damages for delay when a construction contract is terminated?
- Do liquidated damages clauses survive/apply?
- If so, is the Employer entitled to payment up until the point of termination or beyond?
- There are 3 potential outcomes when a Contractor fails to complete the works and a second contractor steps in:
 - i. The liquidated damages clause does not apply at all;
 - ii. The clause only applies up until the point of termination;
 - iii. The clause applies until the second contractor achieves completion.

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

- The commonly accepted position (recorded in most leading legal textbooks) had been that the Employer was entitled to:
 - i. Recover liquidated damages for delay at the contractual rate up to the date when the contract is terminated; and
 - ii. General damages thereafter.
- This is no longer regarded as the default.

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

Triple Point Technology, Inc. v PTT Public Company Ltd [2019]
EWCA Civ 230

- The liquidated damages clause in that case (Article 5.3) provided that:

“If CONTRACTOR fails to deliver work within the time specified and the delay has not been introduced by PTT, CONTRACTOR shall be liable to pay the penalty at the rate of 0.1% (zero point one percent) of undelivered work per day of delay from the due date for delivery up to the date [PTT] accepts such work...”

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

- The clause in question (Article 5.3) was focused specifically on delay between the contractual completion date and the date when **Triple Point** actually achieved completion.
- It had no application to the situation in which the contractor never in fact handed over completed work to the employer.
- Therefore it was held that as the Contractor's employment had been terminated before the works had been completed, liquidated damages cannot be applied.
- Whether or not liquidated damages apply therefore very much depends on the precise wording of the liquidated damages clause in question.

Construction Disputes and Insolvency

LIQUIDATED DAMAGES

- However, it is likely that where the wording of the clause links the application of liquidated damages to practical completion by the initial Contractor (as is the case under many industry standard forms of contract such as the JCT) then the liquidated damages clause will not apply at all in circumstances where the initial Contractor's employment is terminated prior to practical completion.
 - E.g. clause 2.27 of the JCT D&B 2016
- This does not mean that the Employer is left without remedy. The Employer can claim damages in the usual way by proving the actual loss it has suffered by reason of the delay rather than the pre-agreed LADs.

Construction Disputes and Insolvency

RETENTIONS

- Retentions are deductions (commonly 5%) from sums due to a contractor or subcontractor.
- Generally held to provide security in respect of the contractor's performance before and after practical completion.
- Under the JCT Design and Build Contract, half the retention is released on practical completion with the remainder held until end of Rectification Period and released following issue of the Notice of Completion of Making Good.
- Much debate and discussion in the construction industry regarding the potential abolition of retentions, or introduction of a scheme to ringfence retentions.

Construction Disputes and Insolvency

ANY QUESTIONS?