HFW

CONSTRUCTION BULLETIN
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Welcome to the March 2020 edition of our Construction Bulletin.

In this edition we cover a broad range of recent developments in international construction law, as follows:

- Court Limits Restitutionary Remedies where a Principal Repudiates a Contract
- Company in Liquidation Can Pursue Adjudication in Narrow Circumstances
- Adjudication for the Offshore Sector
- New Bill to Tackle Unfair Payment in the UK

The inside back page of this bulletin contains a listing of the events at which the members of the construction team will be speaking over the upcoming months.

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"Where contractors have accrued rights at the date of termination, they are limited to enforcing those rights as a debt or claiming contractual damages."

COURT LIMITS RESTITUTIONARY REMEDIES WHERE A PRINCIPAL REPUDIATES A CONTRACT

The Australian High Court in *Mann v Paterson Constructions Pty Ltd [2019] HCA 32* has clarified the remedies available to a contractor if a principal (i.e. employer/owner) commits a repudiatory breach which the contractor accepts.

Previous position

Remedies in restitution are usually only available where there is no contract between the parties. However, prior to *Mann*, in Australia if a principal committed a repudiatory breach of contract which the contractor accepted, the contractor could choose either to make a claim for contractual damages or in restitution. Claims in restitution were available as the courts had held that the contractor was entitled to treat the original contract as void "ab initio" upon repudiation, meaning as if it the contract had never existed.[1] This enabled contractors to recover based on the "reasonable value" of its unpaid work (known as recovery on a "quantum meruit" basis).

This position in Australia was not without criticism, as it in effect entitled the contractor to treat termination as rescission of contract, essentially allowing contractors to unwind the contractual bargain. As a result, contractors often used claims in restitution to increase their claims for work done, over and above the contract price.

Decision in Mann

The High Court has narrowed the availability of restitution as a remedy, unanimously determining that a principal's repudiation does not entitle contractors to treat the contract as void "ab initio".

The High Court held that, where contractors have accrued rights at the date of termination, they are limited to enforcing those rights as a debt or claiming contractual damages. For example, where the contract provides for staged payments and certain stages have been completed as at the date of termination for repudiation, the contractor can only claim in debt or for contractual damages in relation to those completed stages. It can no longer elect to claim in restitution.

Unfortunately, the High Court was split in determining when claims in restitution **are** available to contractors. The majority (four justices) determined that the contractor **might** be entitled to make restitutionary claims in respect of works that had been commenced but not completed prior to termination. However, the majority were split as to the basis for such claims becoming available.

The majority also held that, where restitutionary claims are available, the contract price will act as a ceiling on the sum recoverable in restitution, save for exceptional circumstances. Unfortunately, the majority did not resolve how adjustable contract prices may affect the ceiling on claims in quantum meruit or in what circumstances the ceiling would be lifted.

Mann has brought some certainty for principals facing claims from contractors in Australia, as it has greatly reduced the availability of claims in restitution where the contract has terminated due to the principal's repudiation. This could affect the contractor's approach to a principal's repudiatory breach of contract. Unfortunately, it remains uncertain as to when claims in restitution are available and the extent to which the contract price acts as a ceiling on claims.

In English law, the pre-*Mann* concept that a contractor could elect to bring a claim in restitution or for damages if it accepted a repudiatory breach, never had the same traction as in Australia.[2] Following *Mann*, it would appear that the two jurisdictions are more aligned on this issue.

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1 See, for example: *Sopov v Kane Constructions Pty Ltd (No. 2) [2009] VSCA 141; Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234

2 *Robert Taylor v Motobility Finance Ltd [2004] EWHC 2619 (Comm)*

COMPANY IN LIQUIDATION CAN PURSUE ADJUDICATION IN NARROW CIRCUMSTANCES

Two recent English Court decisions have provided useful guidance on the 'exceptional circumstances' in which a company in liquidation might be able to pursue and enforce an adjudication.

There has long been a tension between the mandatory set-off provisions under the Insolvency (England and Wales) Rules 2016 (Insolvency Rules) – which provide for an automatic set-off of any claims and cross-claims between the company and a creditor, to take effect upon a company entering into liquidation where there have been 'mutual dealings' – and the statutory right of parties to a construction contract to adjudicate disputes at any time.

This tension was recently considered by the Court of Appeal in *Bresco Electrical Services Ltd (In Liquidation) v Michael J Lonsdale (Electrical) Ltd* (Bresco).[1] The Court held, overturning the first instance decision, that a company in liquidation is not precluded by the Insolvency Rules from pursuing an adjudication.[2] However, it held that there is nonetheless a basic incompatibility between adjudication and the regime under the Insolvency Rules. The Court held that it would be futile to pursue an adjudication in circumstances where the adjudicator's decision was incapable – for instance, due to the existence of a cross-claim – of being enforced by the court. As such, the Court upheld an injunction preventing the adjudication from proceeding.

Therefore, whilst a door was finally opened for a liquidator to refer disputes to adjudication, the Court recognised it would only be in 'exceptional circumstances' that a company in liquidation (and facing a cross-claim) could succeed in adjudication, obtain a summary judgment and avoid a stay in execution.

Subsequently, in *Meadowside Building Developments Ltd (in liquidation) v 12-18 Hill Street Management Company Ltd*[3] (Meadowside) the Technology and Construction Court, in considering an application for summary judgment to enforce an adjudication award, provided some clarity as to what might constitute the 'exceptional circumstances' referred to in *Bresco*.

Noting the liquidator's statutory obligation to collect the companies' debts, the Court held that a case is likely to be 'exceptional' where:

- the adjudication determines the final net position between the parties under the contract in accordance with Rule 14.25 of the Insolvency Rules (that is, there are no cross-claims or 'mutual dealings' under any other contract); and
- adequate security is provided in respect of any sum awarded in the adjudication and any adverse costs order which may be made against the company in an enforcement action or subsequent litigation or arbitration.

Following *Bresco* and *Meadowside*, it appears that a liquidator can – at least for now – refer a straightforward dispute to adjudication, provided it is to determine the final net position between the parties and satisfactory security is provided. However, such a case will be exceptional. Where there is a cross-claim under another contract, the adjudication should not be pursued. Note that the position as set out here differs slightly in other jurisdictions. For instance, in Australia courts have recently not permitted an insolvent contractor to pursue adjudication and made clear that set-off under insolvency legislation trumps any right to payment awarded in an adjudication.

Bresco is presently on appeal to the Supreme Court. Watch this space for future developments.

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"A liquidator can...refer a straightforward dispute to adjudication provided it is to determine the final net position between the parties and satisfactory security is provided."

1 *Bresco Electrical Services Ltd (In Liquidation) v Michael J Lonsdale (Electrical) Ltd* [2019] EWCA Civ 27.

2 In *Michael J Lonsdale (Electrical) Limited v Bresco Electrical Services Limited (In Liquidation)* [2018] EWHC 2043 (TCC) Justice Fraser held that an adjudicator did not have jurisdiction where the (England and Wales) Rules 2016 applied.

3 *Meadowside Building Developments Ltd (in liquidation) v 12-18 Hill Street Management Company Ltd* [2019] EWHC 2651 (TCC).

CHRIS PHILPOT
SENIOR ASSOCIATE

"Adjudication stands out as offering the quickest and most cost-effective method to recover financial costs during offshore projects."

ADJUDICATION FOR THE OFFSHORE SECTOR

As the number of offshore projects in the UK and worldwide increases – is it time for the offshore industry to embrace the advantages of adjudication as means of resolving disputes?

Adjudication offers a quick and relatively cheap dispute resolution process that has become invaluable to contractors seeking to protect their cash flow in an increasing competitive construction industry. By contrast, litigation or arbitration invariably take years to complete, are expensive and drain management time and resources.

Despite the benefits of adjudication, the offshore construction industry has been slow to adopt adjudication as a means of dispute resolution. This may simply be because the statutory adjudication regime for construction contracts does not extend to the construction of many offshore structures, including wind farms.[1] However, we have heard many voices within the offshore industry raise concerns as to whether adjudication can ever provide an appropriate forum for the resolution of, what are often, complex technical disputes.

This article considers the key concerns within the offshore industry and explains why adjudication can in fact often be the most attractive dispute resolution process for offshore projects.

Key concerns surrounding adjudication

Offshore construction poses a range of challenges that, whilst similar to those encountered in onshore works, are particular to construction offshore. These principally include management of "known unknowns" (including waiting on weather and unforeseeable seabed conditions) and resource restraints, such as availability of specialist equipment and vessels. This can make disputes arising from offshore projects more complex than onshore projects, as they often involve a number of interrelated factors that contribute to delay or unexpected changes to works.

This has caused some in the offshore industry to question whether adjudication is the correct forum for dispute resolution. The key concerns often raised are:

1. The 28-day adjudication process does not allow sufficient time for proper consideration of complex issues typically involving large volumes of technical documents relating to specialist marine operations often supported by expert and witness evidence from industry specialists.
2. Only a single 'dispute' can be referred to adjudication not multiple 'disputes'. This means parties will need to engage in multiple adjudications which can be more time consuming and expensive than a single piece of litigation.
3. The adjudicator will not have the relevant expertise to understand and correctly decide disputes arising from offshore construction. The adjudicator is therefore likely to get the result wrong.
4. Adjudication awards are interim binding so they can be easily challenged, leading to additional unnecessary time and expense.

We will consider each of these concerns in turn.

The 28-day timetable is unsuitable

The Courts have long recognised that adjudication is an appropriate forum to resolve complex disputes and is quick to dismiss the idea that adjudication is the wrong forum for complex claims. In *CIB Properties v Birse Construction* the court noted that the focus should be on whether the adjudicator is able to reach a fair decision within the time limits imposed, or as otherwise agreed by the parties, rather than whether adjudication was suitable for resolving high value complex disputes.[2]

Whilst the 'standard' statutory timeframe for adjudications is 28 days, if a complicated dispute has arisen between the parties and the referral includes a substantial volume of documents and expert and witness evidence, it is unrealistic to pretend 28 days would allow sufficient time for the claim to be considered properly. However, in these scenarios the parties will agree that the timescale for adjudication should be extended. This could be by 6 months or such other suitable timescale to allow

sufficient time for a response, reply and rejoinder to be prepared. The parties may also agree, or the adjudicator may direct, that a hearing should take place to allow witness and expert evidence to be tested.

It will undoubtedly be in both parties' best interests to agree a sensible timescale for the adjudication so that the adjudicator has time to give proper consideration to the issues in dispute and arrive at the correct decision.

Only a single dispute can be referred to adjudication

Whilst the 'usual' rule for adjudications is that only a single dispute can be referred, this can be easily overcome by including a provision in the contract that allows more than one dispute to be referred to adjudication if the parties agree, or the employer consents.

If this term was not agreed there would be the prospect of multiple adjudications or a concurrent arbitration, which would not be in either parties' interest. Consequently, both parties are likely to agree such a clause.

An adjudicator with no relevant experience may be appointed so you are likely to get the wrong decision

A common misconception is that parties have no control over the adjudicator's appointment so there is a risk of an inexperienced, unqualified adjudicator being appointed to oversee the dispute.

This concern is easily overcome by the parties naming suitable adjudicators in the contract to hear any dispute. The named adjudicators will be suitably qualified and experienced in the world of offshore construction, and well-versed in the technical nature of the disputes that can arise.

It is of course in both parties interests to have a suitably qualified adjudicator named in the contract so reaching agreement with the employer or contractor should not prove challenging.

Adjudication decisions are not final

Adjudication awards are interim binding, i.e. they are generally binding until finally determined by legal proceedings depending on the terms of the contract. What is the point of participating in a process that is 'interim binding' and can be overturned?

This concern has little foundation. In reality, approximately 80% of all adjudication decisions are accepted by both parties and not challenged. The most likely reason for this is that the decision reached is often the correct decision, or not so wrong as to be easily open to challenge. The second is that adjudication awards are enforceable in the Technology and Construction Court and will be upheld unless there are narrowly defined concerns with the way the adjudication was conducted. The parties therefore have relative certainty that if they engage in an adjudication they will receive an enforceable decision that is unlikely to be challenged.

Nevertheless, if a party does feel aggrieved with the adjudicator's decision, it remains open to that party (most probably after paying the adjudicator's award) to start a claim in court or an arbitration to challenge it. It is therefore ultimately open to either party to seek to overturn an adjudication award, but the number of challenges are relatively rare.

Growing support for adjudication in the offshore industry

There is growing recognition within the offshore sector that adjudication has advantages over litigation or arbitration. This can be seen from the new LOGIC[3] and BIMCO[4] decommissioning standard form contracts that now provide adjudication as a means of dispute resolution.[5] This important step reflects the genuine benefits of adjudication providing quick, relatively cheap and private dispute resolution.

It will be interesting to see whether other standard form contracts for offshore works – including LOGIC General Conditions of Contract for Marine Construction and BIMCO wreck removal suite of contracts – will follow suit. We see no reason why they should not.

Conclusion

With demands for projects to be completed in shorter timescales and increasing pressure on contractor profit margins, adjudication stands out as offering the quickest and most cost-effective method to recover financial costs during offshore projects.

It is time for a sea change in opinion and approach to resolving offshore disputes with the industry embracing adjudication.

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1 Staveley Industries v Odebrecht Oil & Gas Services (2001) 98(10) L.S.G. 46, TCC.

2 (2004) EWHC 2365 (TCC).

3 Sub-clause 36.2(b) LOGIC General Conditions of Contract for Offshore Decommissioning Edition 1 - December 2018.

4 BIMCO DISMANTLECON, see more detail at https://www.hfw.com/Dismantlecon.

5 Sub-clause 36.2(a) of the LOGIC General Conditions of Contract (including Guidance Notes) for Offshore Decommissioning Edition 1.

JOANNE BUTTON
ASSOCIATE

"This bill would provide substantial additional protection and avenues of recourse for SMEs subjected to unfair payment practices in the UK."

NEW BILL TO TACKLE UNFAIR PAYMENT IN THE UK

A new private members bill was proposed in the House of Lords on 21 January 2020, to improve payment security for small and medium-sized enterprises (SMEs).

Labour peer, Lord Mendelsohn introduced the "*Small Business Commissioner and Late Payments etc Bill 2019-20*", following representations from the Specialist Engineering Contractors' Group and other industry bodies.

The bill incorporates a number of measures designed to combat payment abuse, at a time when insolvencies in the construction industry are on the rise.

It seeks to amend the Late Payment of Commercial Debts (Interest) Act 1998 by reducing the period from when statutory interest starts to run from 60 to 30 days after the agreed payment date.

It introduces an option for SMEs to refer payment disputes to the Small Business Commissioner (whose remit is expanded to include construction), as a cheaper alternative to adjudication. Although adjudication will still be an option, for more straightforward disputes SMEs may favour a referral to the Commissioner, which could offer a more streamlined and cost effective resolution of the dispute.

The bill gives the Small Business Commissioner powers to impose penalties on large companies who are serial late payers or who provide false payment performance data. It also seeks to outlaw certain unfair payment practices including clauses which prevent a supplier from ceasing work in the event of non-payment, demanding discounts for prompt payment of invoices and charging contractors to get (and stay) on preferred supplier lists.

The bill requires the Small Business Commissioner to publish ranked payment performance data for large businesses and public contracting authorities, in effect naming and shaming companies with a poor payment record.

In addition, the bill seeks to mandate the use of project bank accounts for public sector works worth over £0.5 million.

When announcing the bill, Lord Mendelsohn said "*Late payment is crippling small businesses whilst the UK economy is crying out for investment.*" He hopes that the bill "*will tackle the issue once and for all with a package of measures that is operable, impactful and measurable*".

Some may argue that the bill does not go far enough. It does not ensure compensation for late payment is automatically added to late payments nor does it update the rates of compensation, which have not been increased since they were introduced in 1998. It does not deal with cash retentions.

There are still many hurdles to be overcome before the bill could be enacted. It has had its first reading but it still faces two further readings and a consultation period in the House of Lords and then three further readings in the House of Commons before it could become law. The date of the second House of Lords reading is yet to be announced.

However, if enacted, this bill would provide substantial additional protection and avenues of recourse for SMEs subjected to unfair payment practices in the UK.

Although this bill would only apply to UK construction projects, late payment is an issue which arises on many of the international projects on which we advise. The bill is a timely reminder of the importance of contractors negotiating clauses which provide adequate protection against late or non-payment in their contracts.

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LIST OF UPCOMING EVENTS

RenewableUK Offshore Wind Member Forum
London, HFW Offices
6 April 2020

Offshore Decommissioning Congress
Rotterdam
21 - 23 April 2020
Presenting: Richard Booth

Pre-summer Garden Party
London, HFW Offices
20 May 2020

Kuwait Construction Contracts Forum Event
Kuwait
2 June 2020
Presenting: Michael Sergeant, James Plant, Kijong Nam

Construction Insurance Seminar
Paris
June 2020
Presenting: Ben Mellors

Asia ADR Week
Kuala Lumpur
18 - 20 June 2020
Presenting: Nick Longley

Construction Seminar
London, HFW Offices
22 & 24 September 2020
Presenting: Max Wieliczko, Michael Sergeant, Ben Mellors, Richard Booth

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