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The construction & energy law specialists

Dispatch highlights some of the most important legal developments during the last month, relating to the building, engineering and energy sectors.

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Dispatch

Application of *Bresco* principles

John Doyle Construction Ltd v Erith Contractors Ltd

[2020] EWHC 2451 (TCC)

We reported on the Supreme Court decision in the *Bresco* case in *Issue 241*. The case here was adjourned to be heard after that decision was handed down. JDC, who had been in liquidation since June 2013, made a claim for the summary enforcement of an adjudicator's decision. The claim was for sums JDC claimed to be due on its Final Account for hard landscaping works before the 2012 Olympic Games. (And, it should be noted, the Judge questioned whether the streamlined, fast-track TCC procedure for enforcement of decisions was designed to deal with issues that arise where decisions are, like this one, years, not months, old.) JDC commenced the adjudication in January 2018, claiming approximately £4 million, a sum the adjudicator reduced to £1.2 million.

In August 2016, the liquidators contacted Henderson Jones ("HJ") whose primary business was described as being to "purchase legal claims from insolvent companies". Under the agreement:

- HJ paid JDC £6,500 for the assigned claims, with a further payment to JDC dependent upon outcome;
- HJ had conduct and control of any proceedings pursued in relation to the assigned claims;
- Recovery of any claims was to be paid to HJ;
- 45% of net recovery in those subsequent proceedings (meaning recovery less costs) was to be paid out to JDC by HJ.

Mr Justice Fraser explained that following *Bresco*, the principles to be applied when considering summary enforcement in favour of a company in liquidation are:

- Whether the dispute is one in respect of the whole of the parties' financial dealings under the construction contract in question, or simply one element of it.
- Whether there are mutual dealings between the parties that are outside the construction contract under which the adjudicator has resolved the particular dispute.
- Whether there are other defences available to the defendant that were not deployed in the adjudication.
- Whether the liquidator is prepared to offer appropriate undertakings, such as ring-fencing the enforcement proceeds, and/or where there is other security available. In *Meadowside* (see Issue 233) three mechanisms of security were considered: undertakings by the liquidators; a third party providing a guarantee or bond; and After the Event (ATE) insurance.
- Whether there is a real risk that the summary enforcement of an adjudication decision will deprive the paying party of security for its cross-claim.

With particular regard to the first point, the Judge noted that small disputes, or tightly defined disputes which had been referred for tactical reasons, would not, if the referring party is in liquidation, be suitable. This would mean that "*the type of overly-technical dispute concerned with services of notices within particular number of days that are called 'smash and grab' adjudications would rarely if ever ... be susceptible to enforcement by way of summary judgment by a company in liquidation*". The decision of the adjudicator would have to resolve (or take into account) all the different elements of the overall financial dispute between the parties. So where, as here, the dispute referred was the valuation of the referring party's final account, summary judgment would potentially be available.

The mere fact that a responding party has a claim on another contract, or arising under other mutual dealings, against the party seeking to enforce its adjudication decision, was not itself sufficient to defeat enforcement. It would depend on the size of the claim. Here there was a small claim of £40k on another project. That was not enough. The "real battleground" here was whether there was a real risk that the summary enforcement of an adjudication decision would deprive the paying party of its right to have recourse to that claim as security for its cross-claim.

JDC sought to rely upon what was said to be a draft letter of credit from HJ's bankers, and an ATE policy. Mr Justice Fraser said that the primary concern, when considering whether there was a real risk that summary enforcement of the adjudicator's decision would deprive the paying party of security for its cross-claim, was recovery of the sum paid by way of satisfying the adjudicator's decision. A secondary concern was the costs incurred in winning the money back. Both of these concerns could, in theory at least, be met by appropriate safeguards. Here, no undertakings at all were offered from the liquidators. No ring-fencing was available, so no security was offered by the liquidators in any respect. JDC relied upon security from HJ which was said to provide "reasonable assurances" to Erith that, should it successfully overturn the adjudicator's decision in later proceedings, JDC would be able to (i) repay the capital sum and (ii) meet any adverse costs orders.

This security was said to be by way of letter of credit, and an ATE insurance policy. The former was to deal with recovery of the sum awarded in the adjudication; the latter was to deal with the litigation costs. Erith relied upon the agreements that JDC and the liquidators had with HJ under which HJ retained at least 55% of the sums recovered including any costs recovery. This prima facie would contravene Regulation 4 of the Damages Based Agreements Regulations 2013 and hence be unenforceable.

For the Judge, it was the quality of the security that was of central importance. Here, there was no letter of credit available. Instead there was "a so-called letter of intent" from HJ's bankers. This led to a number of difficulties. For example, the bank's letter required the whole judgment sum to be paid to HJ when about 45% of that belonged to the liquidator. There was no evidence of the bank's own detailed conditions for granting letters of credit, which HJ would have to satisfy. JDC were effectively accepting that no security was available but also saying that HJ would provide it. But HJ said it would only provide it if Erith paid over the money, and even then, all HJ could do was promise to apply for it.

This did not equate to any safeguard that sought to place Erith in a similar position to the one which it would be in were JDC solvent. The Judge then turned to the security said to be available in respect of Erith's costs. Here, the ATE cover available was not sufficient. Again, it would not place Erith in a similar position to that which it would occupy were JDC solvent. The result of this was that the security available (or which was said to be potentially available, were the judgment sum to be paid to HJ) was insufficient and the summary enforcement application was refused.

The Judge stressed that this did not mean that no company in liquidation could ever enforce an adjudicator's decision in its favour. Liquidators may offer appropriate undertakings, such as to ring-fence any enforcement proceeds. These would be powerful points in a claimant's favour on an enforcement application. There were also a variety of different methods and models available to liquidators. Simply because one party to a construction contract is in liquidation, this does not entitle the other party to that contract to a windfall. The enforcement here fell on its own facts.

Omission of Works: NEC3

Van Oord UK Ltd v Dragados UK Ltd

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Dragados was employed as the main contractor in a project for the design, management and construction of a harbour expansion project in Aberdeen. By an agreement, incorporating NEC3 option B, Dragados subcontracted the soft dredging works to Van Oord. However, Dragados entered into subcontracts with two other subcontractors. These both included an area of soft dredging works which also formed part of the scope of the work under Van Oord's subcontract. Van Oord did not know about this prior to the commencement of the court proceedings. Van Oord began dredging work in May 2018. In the course of 2018 and 2019, Dragados issued various Contractor's Instructions to omit certain areas of soft dredging from Van Oord's works. This work was transferred to the other subcontractors.

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In terms of the NEC3 contract, each omission of works constituted a compensation event. The effect of a compensation event on the sum payable under the contract was calculated not under reference to sums in the bill of quantities but rather under reference to Defined Cost. According to Dragados, this resulted on each occasion in a reduction of the total amount payable to Van Oord that it still had to carry out under the contract. Those reductions were given effect by a reduction on each occasion in the bill rate payable by Dragados for Van Oord's remaining work.

So was the transfer of work from Van Oord to the other subcontractors a breach of contract? Van Oord relied on the case of *Abbey Developments Ltd v PP Brickwork Ltd* [2003] EWHC 1987, where the court said that there was no absolute rule of law prohibiting transfer of work to another contractor in any circumstances. The question of whether works could be "omitted", i.e. removed from the scope of the contract, whether transferred to another contractor or not, depended upon the proper interpretation of the contract.

Van Oord said that here there was no provision permitting such transfer. By clause 14.3, the parties had expressly agreed circumstances in which Dragados could instruct that work be omitted, even if it was transferred to someone else to carry out, namely where the project manager under the main contract had issued a corresponding instruction. The parties had further agreed by inclusion of clause 60.1(21) that the issuing by Dragados of such an instruction was a compensation event. It was not suggested that there had been any corresponding instruction issued under the main contract and accordingly those subclauses had no application to the circumstances here. Dragados' purpose or motive was irrelevant.

Van Oord further said that the removal of work from the scope of its works and its transfer to the other subcontractors was a breach of Dragados' obligation under clause 10.1 to act in a spirit of mutual trust and cooperation. Without informing Van Oord of its intention at the time of entering into the subcontract, Dragados had "triple-contracted" in relation to approximately one third of Van Oord's works.

Dragados said that the removal of work from the scope of works was not a breach of contract. By means of the compensation event mechanism, NEC3 provided a fair and adequate procedure to compensate a subcontractor for omissions, with the purpose of ensuring that the subcontractor was neither better nor worse off as a result. Instruction of an omission should not therefore be regarded as a breach of contract.

Lord Tyre summarised the PP Brickwork case in this way:

- *"A contract for the execution of work confers on the contractor not only a duty to carry out the work but a corresponding right to complete the work which it contracted to carry out.*
- *A clause entitling the employer to vary the works must be construed carefully so as not to deprive the contractor of his contractual right to the opportunity to complete the works and realise such profit as may then be made. Clear words are needed if the employer is to be entitled to remove work from the contractor in order to have it done by somebody else.*
- *There is no principle of law that says that in no circumstances may work be omitted and given to others without incurring liability to the original contractor. The test is whether, on a proper interpretation of the contract read as a whole, the clause relied upon by the employer is wide enough to permit the change that was made.*
- *The employer's motive or reason for instructing the omission of the work is irrelevant."*

Applying those principles to the circumstances here, the question for the Judge was whether the terms of the subcontract entitled Dragados to omit works from the scope of the subcontract works and have them carried out instead by another party. Lord Tyre did not consider that there was a clear contractual entitlement to omit works and transfer them to another subcontractor in the way Dragados had done here. By expressly providing for a particular situation in which Dragados was entitled to give an instruction to omit work, that raised an inference that in other circumstances Dragados was not so entitled.

The Judge made it clear that he had reached this conclusion without having to place any significant weight upon clause 10.1. Given that the motive for omitting the works was irrelevant, it was not necessary in this context to inquire into whether the omission of the works amounted to a breach of the obligation under clause 10.1 to act in a spirit of mutual trust and cooperation.

In terms of the NEC3 contract here, the omission of work did constitute a breach of contract. And the contract then went on to specify the remedy – and indeed the only remedy – available for a breach of contract, namely that it was a compensation event.

Dispatch is produced monthly by Fenwick Elliott LLP, the leading specialist construction law firm in the UK, working with clients in the building, engineering and energy sectors throughout the world.

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