Fenwick Elliott

The construction law specialists

RICS Legal Issues in Construction - JCT contracts

by Simon Tolson

In this paper I shall address:

- A lawyer's view on the applicable English law on sustainable development
- An update on payment law and construction contracts juxtaposed to the changes in 2009
- Summary of the JCT 2009 Revisions to payment etc
- Common legal myths with JCT on "snagging"
- Sectionalisation completion and time at large
- Disputes and 2009 and pinch points for JCT contracts in a recession

A lawyer's view on the applicable English law as it sits around that leviathan, sustainability/sustainable development

1. Sustainable development has a diversity of meanings to different folk depending on the participant you speak to for a view. Sustainable development does not just mean diminishing the carbon footprint of a person, company or nation. Sustainable development has become a concern everywhere for the construction industry. Hitting my Google search button produced no less than 24,900,000 international hits and 1,840,000 domestic ones! Such is the mass of material written on the subject, from so many interest groups and viewpoints, it is hard to know where to start.

2. Indeed, if you had invited a lawyer just a few years ago to tell you what he understood about sustainable development, and whether he would know a sustainable argument from an unsustainable one, there would be a scratched chin and a ruffled brow or two. Today particularly in my field a straw poll would elicit rather more thanks to the journalistic profession, regulators and the fashionista designers who are running with the sustainable ball. The UK Climate Projections 2009, based on Met Office science, illustrate the extent of the changes the UK might face (unless this is all about sunspots[1]) in the absence of global action to cut emissions – warmer and wetter winters, hotter and drier summers, increased risk of coastal erosion and more severe weather. The maps and findings are publicly available online. The doomsayer scientists all say we are standing on a precipice. One thing I am quite sure of is that sustainable provisions will become more and more prescriptive with time, so mark my words.

3. We are fortunate that the UK has world-class climate change research institutions and consultancy services in carbon measurement and management, but it is the 'doing' that counts!

4. The type of sustainability I am referring to is about making sure all of our businesses and governmental bodies, public services, national resources, and economy have the means to continue in the years ahead at a micro and macro level. The built environment is said to account for around 47% of CO_2 emissions in the UK, with a significant proportion of this relating purely to the running and operating of existing buildings and their facilities. It is a highly emotive subject as we are being forced to wake up to the fact that there are limits to the natural resources available

1. Sunspots are dark, cooler patches on the Sun's surface that come and go in roughly an 11-year cycle, first noticed in 1843. They have gone away before as they have now! They were absent in the 17th century – a period called the "Maunder Minimum" after the scientist who spotted it. Crucially, it has been observed that the periods when the Sun's activity is high or low are related to warm and cool climatic periods. The weak Sun in the 17th century coincided with the so-called Little Ice Age. The Sun took a dip between 1790 and 1830 and the earth also cooled a little. It was weak during the cold Iron Age, and active during the warm Bronze Age. Recent research suggests that in the past 12,000 years there have been 27 grand minima and 19 grand maxima. Throughout the 20th century the Sun was unusually active, peaking in the 1950s and the late 1980s. Dean Pensell of NASA, says that, "since the Space Age began in the 1950s, solar activity has been generally high. Five of the ten most intense solar cycles on record have occurred in the last 50 years." The Sun became increasingly active at the same time that the Earth warmed. But according to the scientific consensus, the Sun has had only a minor recent effect on climate change.

to mankind. Our architects and engineers are ahead of us and amongst the finest at creating designs for the low-carbon cities of the future like Masdar City[2] in Abu Dhabi; others are happening in China[3] and 10 London boroughs.

5. Only in the last few days we have all, I am sure, seen the reports on the flooding in Istanbul, Turkey which show how man's poor infrastructure combines to create far worse climate change issues.

> *"The presence of deadly floods right in the heart of Istanbul first of all points at the insufficient infrastructure of the city," said Dr Filiz Demirayak, the CEO of WWF-Turkey. "Unregulated urban development and infrastructure have become barriers preventing rain water to reach the sea via its natural path."*

6. Climate change is one of the biggest challenges facing the world. Few now doubt that human beings are responsible for most of the recent planetary warming. We are emitting greenhouse gases (most significantly carbon dioxide but methane is not far behind) into the atmosphere much faster than plants and oceans can absorb it. One stark reality is that current consumption patterns of the UK could not be replicated worldwide as this would require three planets worth of resources; we must move to one-planet living. But I am realistic - best practice developers have included sustainability provisions in their contracts for years and they seldom make the final cut. These provisions may well fare as well as the JCT third party rights option and data interchange supplement. Any developer or occupier can already include sustainability in the specification, but unless there is some sanction in the form of amended building regulations or a real cost incentive in terms of whole life cycle costings for buildings, these provisions, if introduced, are likely to remain an aspiration and of dubious enforceability in any case. However, a great deal of this is about changing the way we think and about educating what "value for money" is in its wider context.

7. This is a reflection of man's proficiency in investing in economic resources, yet our society has been less triumphant in looking after the human, social and environmental resources that we rely on. One of the solutions is "sustainable development" and bodies like JCT Limited are doing their bit to encourage this. As Peter Hibberd of the JCT put it, "We owe it to future generations to ensure that the buildings we put up today protect the environment as far as possible - and at the same time are great places in which to live, work and have fun."

8. Sustainable development was famously defined in the Brundtland Report as:

> *"the needs of the present without compromising the ability of future generations to meet their need".*[4]

9. Without wanting to sound like a lay preacher it is about caring, not just about the here and now, but about the long-term well-being - the future - so we may not harm the planet irreparably by doing what we do now. It means not using up resources in our construction projects faster than the planet can replenish or re-stock them and joining up economic, social and environmental goals. No doubt the current credit crunch does not aid this process as businesses struggle to find means to earn revenue without other distractions.

10. The 2008 Climate Change Act made Britain the first country in the world to set legally binding "carbon budgets", aiming to cut UK emissions by 34% by 2020 and at least 80% by 2050 through investment in energy efficiency and clean energy technologies such as renewables, nuclear and carbon capture and storage.

11. While Government has an important role to play in stimulating companies to act through incentives, rewards and the threat of penalties, it is ultimately businesses that will deliver a supply of goods and services that are less damaging and more resource efficient. The $64m question is whether this is best achieved through hard law, soft law[5] or policy.

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2. In September 2009 Masdar Institute of Science and Technology welcomed its first intake of 92 graduate students, representing 22 different nations. The students are part of a two-year Master's programme at the world's first academic institution dedicated to the research of alternative energy, environmental technologies and sustainability.

3. The number of cities in China has increased from 193 in 1978 to 661 in 2005, among which 54 are so-called mega-cities and 84 are large cities, compared with, respectively, 13 and 27 in 1978. By the end of 2006, the urbanisation rate in China was about 43.6% of the population. This rate is rapidly increasing, with 75% of the population estimated to live in cities by 2050.

4. World Commission on Environment and Development (WCED), 1987, p. 43. Norwegian Prime Minister Gro Harlem Brundtland's definition and the concepts expressed in the report Our Common Future identify the dependency of humans on the environment to meet needs and well-being in a much wider sense than merely exploiting resources: "ecology and economy are becoming ever more interwoven – locally, regionally, nationally and globally".

5. Soft law is a term used to describe a quasi-legal function. Soft law can be found in documents, statements, guidelines, codes of conduct, principles, action plans, declarations, resolutions, and codes of ethics traditionally found in the international arena, although it is surfacing in domestic instances as well. The terminology evolved because of the particular function it served. Essentially providing a framework of guidelines and expectations, soft law lacks the "teeth" that real law, or "hard law", can have. Soft law has the potential of becoming "hard law" and morphing into a treaty, contract, or rule of law.

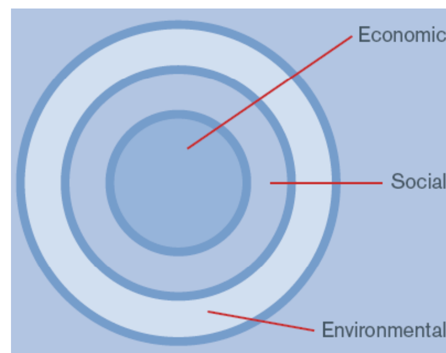
12. Only last week (17 September 2009) the Government announced through Peter Mandelson, at a meeting of the Strategic Forum for Construction, that he was commissioning a review of the construction industry to ensure it was "fit for purpose" for delivering a low carbon future. The review will assess the strengths of and opportunities for the UK construction industry in a low carbon economy and consider how the UK can be a world leader in this sector. This review will be led by the Chief Construction Adviser (to be appointed) and will be undertaken by a mix of industry experts and those with wider business experience. We shall see what happens.

13. The bottom line is learning to live within the earth's natural environmental limits without materially disturbing our wealth or happiness. However, there are in fact three bottom lines.

14. This idea of the "triple bottom line"[6] proposes that an organisation's licence to operate in society comes not just from satisfying stakeholders through improved profits (the economic bottom line), but from improving its environmental and social performance also. As such, it encompasses environmental responsibility, social awareness and economic profitability. There are two accepted schools of thought based on the triple bottom line, the Three Pillars model and the Russian Doll model.

15. The Three Pillars model sees sustainability as the merging of the economic enterprise, social well-being and environmental integrity. In the Russian Doll model, economic activity is at the epicentre as the basis of wealth creation, which drives the development engine but at the same time is constrained by environmental and social conditions. Thus:

Russian Doll



Three Pillars

16. The impression I have painted may create the image of a bunch of open-toed tree-huggers, but this is for "normal" people. Businesses are becoming globally aware that sustainability issues have to be considered within the context of doing business around social and economic hubs, in the same way as factors such as competition rules and procurement policy. One can see and read in the industry journals and

6. First coined in 1994 by John Elkington, the English sociologist, who for the past 30 years has concerned himself with issues of the environment, more recently, sustainability.

quality press that the agenda for change has arrived and our laws and contracts are beginning to reflect this. Even if there is a mismatch in timing between the electoral and environmental impact of change we all know that no one nation on its tod can resolve the problems of global warming and CO_2 emissions. Emissions have no definable boundaries, Chernobyl proved that one. Short of international action commonly agreed and followed through, it is hard even for a large nation to make a difference on its own.

17. In the construction and allied professions given our global dominance (yes even in this crunch), we are uniquely equipped to contribute to improving our credentials as players in more sustainable development[7] as a real selling point. While China and India may make us feel our endeavours make little or no change to the macro picture, even there things are changing.[8] The cynics cannot argue that sustainability is anything but virtuous. The next few decades promise to be amongst the most challenging ever for the civil engineering community. Change is being imposed on world orders with the increasing populations of the Middle East and Asia, progressive urbanisation, and ongoing economic development, not to mention climate change and the persistent risk of extreme events already present. It will no more be I can do it, but I can do it without causing more than minimal impact on the planet; the credentials have changed. International law will catch up with the policy soon enough.

18. It was Edmunde Burke[9] who said "No one could make a greater mistake than he who did nothing because he could do only a little."

19. All the reliable evidence shows the earth is at a critical crossroads. While revolutionary advances in science and technology have lifted humanity and its condition to new heights of prosperity and longevity in many parts of the world, hundreds of millions of people are vulnerable to the impacts of hazards and natural disasters and a host of other challenges. At the same time, human activity, especially in the last 100 years, is threatening the health of the environment and potentially posing risks of unprecedented magnitude to our shared future.

20. With the ever-increasing need to become more environmentally friendly, governments are urging companies to incorporate sustainability at the design process. Three years ago the United Kingdom Government launched its Code for Sustainable Homes,[10] and is moving (slowly) towards all "zero-carbon homes"[11] by 2016 and all new non-domestic buildings are to be zero carbon by 2019. Yes, pigs might fly, but that is the target. On 27 February 2008 the Government confirmed its mandatory rating against the Code for new homes from 1 May 2008. The latest guide came into effect on 3 November 2008.

21. On these shores the UK Government, the Scottish Executive, Welsh Assembly Government, and the Northern Ireland Administration have also agreed upon a set of principles that provide a basis for sustainable development policy in the UK. For a policy to be sustainable, it must respect all five principles:

    (i) Living within environmental limits

    (ii) Ensuring a strong just society

    (iii) Achieving a sustainable economy

    (iv) Using sound science responsibly

    (v) Promoting good governance

22. In terms of focusing its efforts, the UK has identified four priority areas for immediate action, shared across the UK. These are:

7. The Middle East Centre for Sustainable Development (MECSD) is blazing a trail to meet the demand for Green Certified Sustainable Development, in Dubai and across the region. The UAE has turned the corner now that Abu Dhabi is building the first zero-carbon, zero-waste city in the world. The Masdar development in Abu Dhabi is a 6 km sq, car-free "walled-city" scheme. The development is being driven by Abu Dhabi's Future Energy Company and will include a new HQ for the company as well as a new university.

8. In China now, they are hungry to learn how their industries can be made more sustainable; the Chinese were sensitive while all eyes were on Beijing in August last year for the Olympics and saw the smog, rate of economic growth, urbanisation and industrial development, and the unprecedented forces on the country's infrastructure, society, and environment.

9. Politician and philosopher, 1729-1797.

10. On 13 December 2006, the Code for Sustainable Homes - a national standard for sustainable design and construction of new homes - was launched.

11. The Government is consulting, until 18 March 2009 (following criticism from John Callcutt, former head of English Partnerships, in his "Review of Housebuilding Delivery"), on the definition of zero-carbon homes, to apply to all new houses built from 2016. It also seeks views on its ambition that new non-domestic buildings should be zero carbon from 2019. There is to be more detailed consultation on that next year.

(i) Sustainable Consumption and Production – the Government says that to live within our resources, we need to achieve more with less. This requires us to change the way we design, produce, use, and dispose of the products and services we own and consume.

(ii) Climate Change and Energy – the Government says we need to secure a profound change in the way we generate and use energy (we now have more wind turbines than any other country in Europe), and in other activities that release greenhouse gases, to reduce greenhouse gas emissions in the UK and worldwide, whilst at the same time preparing for the climate change that cannot be avoided.

(iii) Natural Resource Protection and Environmental Enhancement – the Government says that understanding the limits of the natural resources that sustain life and our economy is essential, as key industrial sectors are directly and indirectly reliant on functioning ecosystems.

(iv) Sustainable Communities – the Government says its aim is to look after the places in which people live and work, for example by developing green, open spaces and building energy-efficient homes.

23. However, enough of politics and social policy; let us look at the current legal framework and its impact on construction.

Contract, legislation and sustainable development

24. To support the Government's sustainable development policy (which the next administration is likely to follow) there have been a number of EU Directives and statutes passed over the years but all have tended to have more oblique paths to sustainable development since they tend to have broadly environmental roots. The truth is there has been a mass of guidance and policies permeating the industry, but little in the way of primary legislation until now.

25. Yes, we have the Climate Change Act 2008, which became law on 26 November 2008, and it is changing the canvas. Make no mistake, the Act provides a framework for further regulatory action to be rolled out and establishes overarching emission targets for the Government to meet. The Act leads the way in bringing in requirements on business to meet increasingly challenging targets for reducing carbon emissions. The UK has become the first country in the world to introduce legally binding targets to reduce greenhouse gas emissions. The UK Low Carbon Transition Plan plots how the UK will meet the 34% cut in emissions on 1990 levels by 2020, set out in the last budget. According to the Department of Energy and Climate Change we have already reduced emissions by 21% – equivalent to cutting emissions entirely from four cities the size of London. The "10:10" scheme is also an ambitious project to unite every sector of British society behind one simple idea: that by working together we can achieve a 10% cut in the UK's carbon emissions in 2010.[12]

26. The Rt. Hon. Edward Miliband, the energy and climate change secretary, said there are huge commercial and economic opportunities in the new technologies associated with combating climate change. "The world has the potential for an environmental technology revolution - the kind of revolution recently seen in the astonishing growth of information technology."

27. The central points of the Climate Change Act are:

- Legally binding targets: Greenhouse gas emission reductions through action in the UK and abroad of at least 80% by 2050, and reductions in CO_2 emissions of at least 26% by 2020, against a 1990 baseline. The 2020 target will be reviewed soon after Royal Assent to reflect the move to all greenhouse gases and the

12. See: www.1010uk.org/

increase in the 2050 target to 80%. You can bet your boogaloos that legislation will follow in our industry to make this happen.

- A carbon budgeting system which caps emissions over five-year periods, with three budgets set at a time, to set out our trajectory to 2050. The first three carbon budgets will run for 2008-12, 2013-17 and 2018-22, and must be set by 1 June 2009. The Government must report to Parliament its policies and proposals to meet the budgets as soon as practical after that.

- The creation of the Committee on Climate Change, a new independent, expert body to advise Government on the level of carbon budgets and where cost-effective savings could be made. The Committee will submit annual reports to Parliament on the UK's progress towards targets and budgets to which the Government must respond, thereby ensuring transparency and accountability on an annual basis.

- International aviation and shipping emissions - the Government will include international aviation and shipping emissions in the Act or explain why not to Parliament by 31 December 2012. The Committee on Climate Change is required to advise the Government on the consequences of including emissions from international aviation and shipping in the Bill's targets and budgets. Projected emissions from international aviation and shipping must be taken into account in making decisions on carbon budgets.

- Use of international credits - Government is required to "have regard to the need for UK domestic action on climate change" when considering how to meet the UK's targets and carbon budgets.

- The independent Committee on Climate Change has a duty to advise on the appropriate balance between action at domestic, European and international level, for each carbon budget.

- The Government also amended the Bill in its final stages to require a limit to be set on the purchase of credits for each budgetary period, by secondary legislation requiring debate in both Houses of Parliament, and taking into account the Committee's advice.

- Further measures to reduce emissions include powers to introduce domestic emissions trading schemes more quickly and easily through secondary legislation; measures on biofuels; powers to introduce pilot financial incentive schemes in England for household waste; powers to require a minimum charge for single-use carrier bags (excluding Scotland).

- On adaptation the Government must report at least every five years on the risks to the UK of climate change, and publish a programme setting out how these impacts will be addressed. The Act also introduces powers for Government to require public bodies and statutory undertakers to carry out their own risk assessment and make plans to address those risks.

- An Adaptation Sub-Committee of the Committee on Climate Change, in order to provide advice to and scrutiny of the Government's adaptation work.

- A requirement for the Government to issue guidance next year on the way companies should report their greenhouse gas emissions, and to review the contribution reporting could make to emissions reductions by 1 December 2010.

- Requirement also that the Government must, by 6 April 2012, use powers under the Companies Act to mandate reporting, or explain to Parliament why it has not done so.

- New powers to support the creation of a Community Energy Savings Programme, as announced by the Prime Minister on 11 September 2008 (by extending the existing Carbon Emissions Reduction Target scheme to electricity generators).

- New requirement for annual publication of a report on the efficiency and sustainability of the Government estate.

28. What we are seeing is evidence that enabling legislation and guidance will before long turn into hard prescriptive legislation as, if truth be told, sustainability until now has only had lip service paid to it in many projects. Contracts are usually silent on what it means with any specificity, and what is to apply or occur if it is not met. Usually there are no sanctions (i.e. teeth) to bite if un-sustainable construction practice (definition, I know, is not easy) is perpetrated, but I am now seeing BREEAM (Building Research Establishment's Environmental Assessment Method) and LEED (Leadership in Energy and Environmental Design's 'green building' rating systems) standards imposed by contracts as recognised environmental ratings in performance requirements. Many public sector organisations are required to comply with these standards - and many private companies choose to, because of their credibility. Many of my main contractor clients employ both BREEAM accredited assessors on staff, as well as LEED accredited designers.

29. Yet in all this, we see some trends emerging. There is a discernible and increasing trend towards a market requirement for sustainable development and the credit crunch will not obviate this; one can see this particularly amongst the major commercial procurer/developers such as Quintain, British Land, Hammerson, and Land Securities, Canary Wharf, etc. Green developments can be more marketable, particularly where whole-life costing is taken into account,[13] and developers and some clients are now using sustainability as a positive differentiator. Fit-out contractors like Morgan Lovell, Overbury, ISG, Parkeray are also forging ahead in advocating and doing sustainable development in their conversions and fit-out projects.

The Energy Performance Directive and badging

30. The real guts for change here in the UK has come with the Energy Performance of Buildings Directive (EPBD)[14] which requires information about the energy efficiency of buildings to be provided when they are sold, rented out, or constructed, not unlike the label you see when you buy a fridge or dishwasher. It has created a benchmark but a few cynics are querying the point of it. This requirement has been implemented in England and Wales by the Energy Performance of Buildings (Certificates and Inspectors) (England and Wales) Regulations 2007.

- The Energy Performance Certificate - 1 October 2008 marked the final roll-out of Energy Performance Certificates (EPCs) to all building sectors with the introduction of EPCs to rented homes and the extension of EPCs to include all commercial buildings when bought, sold, or rented.

- The Display Energy Certificate - since 1 October 2008 DECs are required for public buildings and those occupied by public authorities which have a total useful area greater than 1000m^2 and provide a public service to a large number of people and are therefore frequently visited by those people (e.g. a school, hospital, government or local authority building). These certificates show the actual energy usage of a building, the Operational Rating, and help the public (if they are sad enough to enquire) to see the energy efficiency of a building. This is based on the energy consumption of the building as recorded by gas, electricity and other meters used by a building over a 12-month period.

13. Essentially, whole-life costing (WLC) is a means of comparing options and their associated cost and income streams over a period. Costs to be taken into account include initial capital or procurement costs, opportunity costs and future costs. Only those options that meet the performance requirements for the built asset should be considered. Awareness of WLC is growing within the UK construction industry. It has been identified as a mechanism to deliver improved value for money and government clients are targeted with using WLC.

14. (2002/91/ EC)

- In addition, since January 2009 new regulations also require that all air-conditioning systems above 250 kW are inspected. Those over 12kW must be inspected by 4 January 2011. This work must be carried out by an accredited inspector. Why? Because M&E is hugely power hungry and set up wrong costs a fortune to run in large buildings.

- Thus, the application now of Energy Performance Certificates[15] (EPCs) to all buildings brings the issue to the fore and we are seeing an increase in "green leases"[16] and covenanted rights and obligations, which affect repair, replacement, and renewal.

31. Energy labelling of buildings has been considered a critical factor in the energy performance of buildings since the late 1990's. So, now we have it. However, as the cynics will know, it's one thing having a label, another thing running the building efficiently. Many costs consultants and building services engineers I have spoken to have remarked on how poor use of control settings, building management systems etc. can wreck the statistics on the EPC ticket. Therefore, people need to be educated too and designers need to have users more clearly in mind when planning their buildings. The fact that the energy efficiency programmes can reduce the energy consumption in the developed nations that are consuming more energy has made it imperative to accomplish the energy labelling procedure worldwide as it creates competition in the right area. G.J. Levermore (2002) has stated that the energy labelling of buildings in developed nations will not only help reduce the energy consumption but also pave the path for achieving an energy efficient economy. We shall have to see if he is right.

The role of contract law in sustainability

32. Contractually, the stage at which sustainability aims need to be addressed is at the start when planning the build – the project feasibility stage. Simply applying the tag "sustainable development" to projects is meaningless unless it is given an explicit meaning, and one which is bespoke to the specific project and to the particular environment in which that project is located. Only once these objectives have been ascertained can they be properly reflected in the employer's requirements/ specification (or the equivalent performance requirement), and carried through into the drafting of the construction contract. Without clear realisable objectives, there is a real danger that the desired outputs will not be met.

33. There are a number of contract-invoked mechanisms for clients to choose from to ensure sustainable best practice. The best and long term ensure that specification and design criteria take account of the long-term sustainability of the project – not just in terms of the design life of materials (e.g. mass concrete versus light frame) but also in terms of the costs of operation and maintenance over the lifetime of the asset. This issue of embodied energy[17] has become an important criterion, i.e. looking at the energy to make the elements of the build not just the output construction. Is the building suitable for its setting? Is it fittingly located? Has the ability of users to pay for long-term operation and maintenance been considered? What about legacy issues? One can see that there are tensions in this because, on an individual project basis, some interests are short term: the contractor's interest outside PFI and facilities maintenance is usually limited to the build period plus defects liability period. The owners' interest may be the next 30 years.

34. It is not always easy adequately to define a sustainability objective in contractual terms. It is also very important that the entire construction team buys into the process (it is part cultural and part educational) and "buy-in" can be achieved through more strict drafting of absolute requirements (so far as possible) referring to supporting documentation for implementation. My belief is that aspirational approaches to sustainable construction are as weak as dishwater and frankly futile. Far better to set out, by revised Conditions and Specifications, what is to be

15. Since 1 October 2008, all buildings whenever sold, built, or rented need an Energy Performance Certificate (EPC) on a scale of A-G. The most efficient, which should have the lowest fuel bills, are in band A. Since 6 April 2008, as far as commercial buildings are concerned, EPCs have been required for their sale, rental, or construction.

16. The concept of "green leases" has been introduced in Australia to address the split incentives, information asymmetry and supply chain issues faced by the commercial office market sector.

A "green lease" is a lease between the landlord and tenant of a corporate building with an additional set of schedules compared with a "normal" lease contract. Green leases include a legal basis for monitoring and improving energy performance, which provides mutual contractual lease obligations for tenants and owners to achieve resource efficiency targets (e.g. energy, water, waste) and to minimise the environmental impacts of an organisation's estate. This ensures that a building operates at an agreed level through regular monitoring and addressing issues as they arise.

17. Embodied energy of a building is the energy used to acquire raw materials and manufacture, transport and install building products in the initial construction of a building. Embodied energy is a new concept for which scientists have not yet agreed absolute universal values because there are many variables to take into account, but most agree that products can be compared with each other to see which has more and which has less embodied energy. Comparative lists (for an example, the Bath University Embodied Energy & Carbon Material Inventory) contain average absolute values, and explain the factors which have been taken into account when compiling the lists.

achieved, such as the requirement for more sustainable products (without vagary) or end solutions like say installing biomass boilers (are they not dirtier?), SUDS,[18] maximising the use of the stack effect to reduce the need for M&E plant, natural and manufactured shade or greywater flushing systems. The social housing sector is already familiar with provisions in building contracts where contractors must comply with the Code for Sustainable Homes or with softer "green" partnering contracts, the latter are often only good until the ink is dry on the contract, and in these hardening times partnering usually goes out the window. A preferable medium of compromise is specific customised contract drafting adopted to incentivise the project team whilst having some bite; it should not impose impossible barriers either on suppliers and their advisers or on the legal community. Here are some non-exhaustive examples to set us off:

(i) Prohibited or deleterious materials clauses are frequently put in contracts and provide an inventory of materials not to be used, or codes and standards to be complied with on pain of some contract penalty. This type of clause can be adapted to include a positive absolute obligation to use sustainable materials, for example softwood from sustainable forests or materials recommended in the BRE Green Guide to Specification (the latest June 2008 edition), which provides guidance on the relative environmental impacts of over 250 elemental specifications.

(ii) Alternatively, a contractor might be given a compensable right to an extension of time for any procurement difficulty in obtaining specified materials or products for the sustainable objectives of a project. A pain/gain share mechanism could be used as on some BAA T5 contracts, with the contractor and design team sharing a monetary benefit if, for example, the development is procured within very specific deliverables, such as finite energy efficiency ratings, reuse of demolition arisings like masonry and cementatious waste, using Forest Stewardship Council (FSC) certified timber or other recycling/waste management targets on things like aggregates and sand. Reducing waste is a huge issue.[19] However, an enlightened client is required.

(ii) There are, of course, also a number of current contractual provisions in many standard form contracts, which can be tailored to address sustainability or ramp up standards like BREEAM or Part L by specified quotients capable of measurement. For example Stanhope is a developer that calls for and has achieved currently in the range 10 – 20% better than Part L 2006.

(iii) Change of law clauses: commonly the risk of any cost impact of a change in legislation sits with the employer in the standard forms but in the real world is often shunted to the contractor and sustainable/green/regulatory changes can be imposed too. In a long-term development project like a PFI hospital, these additional costs can be high, for example mandatory testing and rating for EPCs. Addressing who is best placed to manage this risk at the outset is important, as over say the next three years changes in the law in the sustainability field will inevitably be introduced and will likely be costly to meet, so it is an issue to address at the drafting stage.

(iv) Management and treatment of site waste may also be expressly addressed in the contract. Whilst obviously since 6 April 2008, any construction project worth more than £300,000 in value that is unable to provide evidence of a Site Waste Management Plan (SWMP) can be fined, smaller jobs and larger ones can also include a contractual stipulation to comply with the CIRIA, Construction Waste and Resources guidance on sustainable building and construction waste, and consider more effective use of a SWMP. This process must also identify waste management options including reference to the waste hierarchy, on- and off-site options, and pay particular attention

18. Sustainable Urban Drainage Systems

19. The construction, demolition & excavation (CD&E) sector generates more waste in England than any other sector, and is the largest generator of hazardous waste, around 1.7 million tonnes. By comparison, the sector accounts for 9–10% of GDP.

to arrangements for identifying and managing any hazardous wastes produced.

(v) In addition, there are a number of contractual stipulations that directly or indirectly address sustainability. These range from use of value-engineering and risk register clauses to encourage innovation and efficiency of design, use of "Recycling" or "Wastage" clauses, as hinted above, to promote minimal waste, appointing an Environmental Compliance Officer on-site and instituting systems such as waste management plans, to ensuring procurement of sustainable materials by setting up framework arrangements with particular suppliers. Take, for instance, clause 13.2 of FIDIC Conditions of Contract for EPC/Turnkey Projects (Silver Book), a value-engineering clause. This gives the contractor the option (not the requirement) to:

> *"at any time 'submit a written proposal' which (in the Contractor's opinion) will if adopted, (i) accelerate completion, (ii) reduce the cost to the employer of executing, maintaining or operating the Works, (iii) improve the efficiency or value to the employer of the completed Works, or (iv) otherwise be of benefit to the Employer." [Emphasis added]*

The only difficulty with this condition is that the contractor cannot recover the cost of preparing any proposal. This means that except where the contractor is confident that his proposal will be adopted, there is no real incentive to propose efficiencies. Furthermore, there are difficulties with evaluation of value-engineering provisions as Hoare Lea's recent report on the proposed revisions for Part L in 2010 reveal.[20]

FIDIC resorts to the standard valuation procedure but some of such clauses attempt to evaluate the "benefit" in restitutionary terms to the employer and allow the contractor a percentage share. This is because alterations to design that improve value or efficiency may in fact diminish the capital cost of the project and consequently may result in a decrease in the overall construction cost – again, little enticement to the contractor unilaterally to propose such changes.

(vi) Then there is conditions precedent, which can be added to a contract to introduce something of a contractual sharp stick to certifying PC. One possibility might be imposing the top Energy Star[21] BREEAM standard, i.e. the newest Building Research Establishment Environmental Assessment Method (BREEAM) standard, or Merton Rule Pus[22] as a condition of the certification of practical completion of a project or milestone. So one could make a good score on key elements such as energy efficiency and water consumption compulsory, not optional as they are now. This requirement could be linked to funding requirements or obligations in a lease or development agreement to ensure the contract package is back to back.

(vii) One could also borrow from the world of process engineering performance-related liquidated and ascertained damages if the as-built project was outside stated parameters of efficiency at given constants provided the clause was not construed as a penalty.

(viii) Then there are those provisions requiring contractors to "use all reasonable endeavours" to maximise cost recovery by reusing, recycling, selling, or otherwise commercially exploiting any arisings, waste or reusable process parts which are also becoming more common. Points to observe here are the various criteria to which such provisions are subject (commonly they are qualified with the words: "without derogating from any other obligation of the Contractor under this Contract" and "to the extent permissible by Law and practicable").

20. Hoare Lea's study modelled two 2006-compliant buildings using the trial Part L 2010 software. There were a few surprises, not least its apparent favouring of fan-coil systems over ventilation with passive cooling. There also appears to be some obvious coding errors. Of perhaps greater significance was that, on the buildings modelled, it seemed compliance could only be achieved with renewable energy such as wind or solar, indicating that improvements in energy efficiency are reaching their cost-effective limit.

21. BREEAM Energy Star is the latest addition to the BREEAM family of sustainable building standards, which are continually updated to make new and existing buildings more sustainable and cost effective from cradle to grave.

22. Launched on 1 August 2008, staggeringly the new standard aims to help non-domestic buildings become zero-carbon rated by 2019.

The obligation also tends to be limited to reasonable endeavours rather than absolute ones. Such requirements also need to be clear as to who "owns" the wastage and therefore any financial advantage from recycling. One more factor to think about is cost treatment: in target cost contracts any financial benefit could be treated as a credit, so reducing the overall project cost. Debatably, a better incentive to encourage recycling and low wastage would be to allocate any proceeds 50:50 with the contractor.

(ix) For long-term framework agreements - where the client is procuring a series of projects over a set phase - an employer might also consider using specific environmental Key Performance Indicators (KPIs) to measure overall environmental performance. The main advantage of using KPIs as a measure of performance is that they can be moulded to suit the client's specific requirements, can be adaptable during the term and therefore sensitive to market trends, and can also be framed to reward good performance rather than simply discipline bad performance.

35. With regard to what the standard forms are doing on sustainability, the Joint Contracts Tribunal was the first, through Professor Peter Hibberd's[23] efforts[24], to address this issue in its Framework Agreement three years ago and now into all its suite of contracts since May 2009. Soon we can expect the JCT family to lead with domestic work.

36. In JCT's Building a sustainable future together paper published this May it is interesting that they report that their consultation on introducing sustainability provisions into their contracts revealed 86% of respondents believe that contract clauses must be legally enforceable, with clear remedies for default, otherwise they are likely to be ignored; although it was acknowledged that other sanctions might apply but what benchmarks is the issue. The most often stated sanction being a loss in continuity of work, which in a framework arrangement could be painful.

37. Objective measures are important because parties who enter into contract want certainty, insofar as that is possible. So maybe BREEAM ratings, the Merton Rule and Merton Plus Rule, Site Waste Management Plans, Energy Performance Certificates, Display Energy Certificates and Constructing Excellence's Key Performance Indicators (KPI) could be the way for stipulation and form.

38. From a facilitative standpoint the principal JCT suited contracts for securing sustainability benefits are as follows:

- JCT Framework Agreement 2007 together with an underlying JCT contract e.g. Standard Building Contract, Design & Build Contract
- JCT Constructing Excellence Contract 2005 and its associated Project Team Agreement
- JCT Pre-Construction Services Agreement (General Contractor) 2008
- JCT Pre-Construction Services Agreement (Specialists) 2008, together with another JCT construction contract for the second or subsequent stage
- JCT Consultancy Agreement (Public Sector) 2008.

Standard Form Contracts and sustainability

39. Major steps forward have been made in improving the sustainability of buildings through design, but rather less has been done to address sustainability in terms of product specification and the construction process itself. Thus domestically while in a number of cases Standard Form Contracts having undergone recent rewrites (like NEC), generally they have not taken much account of the need for

[23] General Secretary of the JCT.

[24] By "Exploring ways in which the environmental performance and sustainability of the tasks might be improved and environmental impact reduced". The key issues for the working group will be how far the drafting is taken in defining what is meant by "sustainability" and the extent to which such obligations will be legally enforceable. It seems likely that the drafting will take the form of generic sustainability clauses coupled with specific guidance on implementation.

sustainability - save for JCT. Having said this, there are firm signs that sustainability and the environment is finding its way into standard form construction contracts.

40. As I have mentioned, JCT has published Building a Sustainable Future Together, as a guidance note which is principally concerned with how sustainability in design and construction is provided for in contract documents, and with the 2009 amendments to 2005 (revision 2[25]) it has put sustainability provisions within all its contracts since May 2009.[26]

41. The decision by JCT to tackle sustainability, the first contract authoring body to do so, followed wide consultation with the industry. The development phase involved extensive liaison with the different elements that make up the JCT council, which include RIBA, RICS, BPF, LGA, NSCC, CC and SBCC.

42. I think JCT has got the balance right in not seeking to impose unyielding criteria upon parties, or strict objectives. Instead they introduce a framework under which the contract can encompass sustainability. The guidance document stresses that the client's commitment and the early involvement of the supply chain are essential to achieve sustainability, both in the design and the construction processes. It is not prescriptive.

43. Thus, the contractor is encouraged to suggest economically viable amendments to the employer's requirements which, if instructed as a variation, may result in improvement in environmental performance in the carrying out of the works or of the completed works. The JCT says the contractor shall provide to the employer all the information that he reasonably requests regarding the environmental impact of the supply and use of materials and goods which the contractor selects.

44. These clauses are supported by provisions dealing with performance indicators and value engineering as these, if not essential, are beneficial.

45. The JCT is attempting to provide a contractual framework that will be a constant reminder of the need to address sustainability. The framework recognises that contract conditions play a part but also that documentation will deal with sustainability in other ways, such as within notes and schedules to specifications and drawings. It also acknowledges that each project is unique and each client may wish to set different requirements. As I have already mentioned, most of the cost of a project is determined in the initial stages of design; JCT has understood this fundamental with sustainability. Decisions on sustainability arise both in the design and in the construction processes but the former will invariably have the greater impact.

46. Consequently, the procurement route will determine the sustainability provisions contained within the respective contracts.

47. As noted above, most contracts already include provisions to comply with statute and statutory requirements. Further, the JCT is not starting from scratch when it considers how to incorporate sustainability provisions within its contracts.

48. The JCT Framework Agreement 2007 was therefore the first of a number of sustainability provisions.

49. Clause 16 of the JCT Framework Agreement 2007 provides the following:

> *The Provider will assist the Employer and the other Project Participants in exploring ways in which the environmental performance and sustainability of the Tasks might be improved and environmental impact reduced. For instance, the selection of products and materials and/or the adoption of construction/engineering techniques and processes which result in or involve:*

25. The main purpose of revision 2 is to add the principles adopted by the Office of Government Commerce in the Achieving Excellence in Construction Initiative; to simplify the payment provisions and introduce provisions for a retention bond; and to recognise the increasing importance of sustainability. The form of the contract remains substantially unchanged.

26. Following publication of the Revision 2 version of a contract, the Revision 1 Contract and its 98 equivalent have been withdrawn. Withdrawn contracts are available with an "outdated" watermark through Sweet and Maxwell Document Delivery Service.

.1 reductions in waste

.2 reductions in energy consumption;

.3 reductions in mains water consumption;

.4 reductions in CO_2 emissions;

.5 reductions in materials from non-renewable sources;

.6 reductions in commercial vehicle movements;

.7 maintenance or optimisation of biodiversity;

.8 maintenance or optimisation of ecologically valuable habitat; and

.9 improvements in whole life performance

[Emphasis added]

50. This is explained in paragraph 56 of the guide which states:

In line with the UK strategy for more sustainable and environmentally sensitive construction, the Provider is encouraged to assist the Employer [I agree it is all a bit touchy feely] and the other Project Participants in exploring ways in which environmental performance and sustainability of Tasks might be improved and environmental impact reduced:

- ***reductions in waste** – not only reductions in the proportion and/or volume of materials wasted in the construction process but also the volume of extracted materials, demolition waste etc. which have to be removed from site during the construction process;*
- ***reductions in energy consumption** – not only the energy consumption of the completed works/facility but also energy used during the construction process;*
- ***reduction in mains water consumption** – again, not only the water consumption of the completed product/facility, but also water consumed during the construction process;*
- ***reductions in CO2 emissions** – a goal in itself as well as a measure of success in achieving other environmental objectives such as reductions in energy consumption, reductions in use of materials from non-renewable sources, reductions in vehicle movements; and improvements in whole life performance;*
- ***reductions in materials from non-renewable sources** – an essential requirement of sustainable construction;*
- ***reductions in commercial vehicle movements** - to and from the site of the Task;*
- ***maintenance or optimism of biodiversity** – for instance, if it is necessary to chop down an area of mixed woodland to construct part of the works the Parties should endeavour to replace such area with a similar mix of species, not just an area of homogeneous conifers;*
- ***maintenance or optimism of ecologically valuable habitat** – a comparison of the area of ecologically valuable habitat within the total project site area at completion of the Task as compared with that at the start; and*

- ***improvements in whole-life performance*** *– looking beyond the immediate construction process to the long-term use, operation, maintenance and replacement of the project and/or project components.*

51. The question is, then, how do you ensure compliance with these important provisions? The answer is monitoring with a firm hand. Provision for the monitoring of all parties to the Framework Agreement is provided for in clause 21 and in particular clause 21.4 which states:

    The Employer and Provider will jointly review the Employer's report with a view to:

    .1 Identifying aspects of the Provider's performance which may have been overlooked;

    .2 Identifying aspects of the Employer's performance, or that of other Project Participants, which may have had an adverse effect upon the Provider's performance …

    .4 Identifying any particular aspects or elements of the Provider's and/or the Employer's and/or other Project Participant's performance which could be improved upon; and

    .5 Assessing whether the existing Performance Indicators have proved to be, and are likely to remain until the next assessment, fair, reasonable and appropriate indicators of the Provider's contribution to progress in achieving the Framework Objectives.

52. By setting sustainability as a Performance Indicator the parties to a Framework Agreement can monitor each other's performance and identify when standards are not being met. However, this is all very "soft" law I agree.

53. The problem with such provisions is that they have no teeth. They are merely aspirational rather than stipulative and it has to then be questioned whether there is any point in agreeing to something being non-binding, which is the case with these provisions. Which is why, given the feedback on the JCT consultation, that we may see in the future provision for stipulation like Merton Rule plus 5% in all non-residential projects outside city/town centres?

54. Alternatively, compliance (with benchmarks, maybe Part L plus 15%[27]) could be set as part of the condition for the issuing of the certificate of practical completion/taking over predicated on well-defined criteria or standards provided it was capable of precise meaning and not open to endless argument as to whether it had been achieved.

55. The JCT consultation shows ***sustainability provision generally should be included primarily within the specification and design criteria*** of a project and therefore included in the:

    - Preliminaries
    - Preambles
    - Specification, which may include a measured works section, or
    - Schedule specifically prepared for the project

FIDIC's take on sustainability

56. As for FIDIC, the FIDIC Red Book makes a direct reference to the protection of the environment in clause 4.18 which states:

[27] Buildings account, directly and indirectly for, 44% of the UK's carbon emissions. The Government has long signalled its intention to move to zero carbon buildings, starting with homes in 2016 and finishing with all other buildings by 2019. Building Regulations Part L has an important role in achieving this goal. Part L regulates the carbon dioxide emissions from buildings through the control of energy use in buildings. The requirements are set out in the Regulations, with guidance given in the approved documents. There are separate approved documents for new and existing buildings and for dwellings and all other buildings.

> *The Contractor shall take all reasonable steps to protect the environment (both on and off the site) and to limit damage and nuisance to people resulting from pollution, noise and other results of his operations.*
>
> *The Contractor shall ensure that emissions, surface discharges and effluent from the Contractor's activities shall not exceed the values indicated in the Specification, and shall not exceed the values prescribed by the Applicable Laws.*

57. Also from FIDIC there is a further, more oblique reference to sustainability in clause 13.2 which provides that the Contractor can:

> *at any time [submit a written proposal] which (in the Contractor's opinion) will if adopted, (i) accelerate completion, (ii) reduce the cost to the employer of executing, maintaining or operating the Works, (iii) improve the efficiency or value to the employer of the completed Works, or (iv) otherwise be of benefit to the Employer.*

58. The only difficulty with this condition is that the Contractor cannot recover the cost of preparing any proposal. This means that except where the Contractor is confident that his proposal will be adopted, there is no real incentive to propose efficiencies. Furthermore, there are difficulties with evaluation of value engineering provisions. FIDIC resorts to the standard valuation procedure but some of such clauses attempt to evaluate the "benefit" in restitutionary terms to the Employer and allow the Contractor a percentage share. This is because alterations to design that improve value or efficiency may in fact diminish the capital cost of the project and consequently may result in a decrease in the overall construction cost – again, little enticement to the Contractor to unilaterally propose such changes. Finally, proposing the use of a more costly but sustainable alternative may not be met with a positive response from a client determined to maximise their profit.

Consultant appointments – used as a route to sustainable development

59. Above I have set out the limited requirements placed on Contractors, but what of the other limb of the construction team, Consultants.

60. Almost all Consultant Appointments require that the Consultant enter into a Collateral Warranty which provides for the Consultant to provide its services using the reasonable skill and care of a Consultant in the same field.

61. This general duty then is made more specific and usually addresses the use of deleterious materials, and often is in the following prohibitive form which deliverately does not specify materials:

    (i) Which are deleterious or capable of becoming deleterious when used in a particular situation or in combination with any other material or materials;

    (ii) any substance referred to as being hazardous to health and safety in Ove Arup 1997 Report: 'Good Practice in the Selection of Construction Materials' as may be revised or reissued from time to time;

    (iii) or any other substance not in accordance with British Standards (where applicable) or an equivalent of no less a standard of codes of practice and good building practice as set out in any United Kingdom or any other European publication of a recognised body or institution.

62. This is a very negative definition and perhaps there is room for a more positive provision in Consultant Appointments - say a requirement that the Consultant specify for use materials from the BRE Green Guide to Specification or similar document. However, that is not without controversy it seems amongst the architectural profession.[28]

[28] Much bad feeling seems to be emerging around a recently published guide for specifying sustainable materials. The newly updated BRE Green Guide was released with some fanfare to the market back in June, offering a vital resource to design teams grappling with requirements for the Code for Sustainable Homes and BRE's own environmental assessment method (BREEAM).

The latest version was published online which, apart from saving paper, also allows BRE to update and amend entries. The guide covers 1,300 generic specifications, and also measures the embodied impact of materials and building components for generic building types, using it to assign a single rating, ranging from A+ to E.

So far, so good. However, anything with a green or sustainable moniker is bound to attract controversy, and the Green Guide is no exception. A spat emerged over the ratings given to PVCu windows compared with timber. The former had leapt from a could-do-better C standard in the 1999 version of the guide to a near top-of-the-class A in the new version! Given the origin of plastic – oil - concerns arose over how PVCu had made such a marked improvement.

So the Guide is no panacea.

The shape of things to come – where are we going?

63. Whilst in the past, only lip service was paid to the notion of "sustainable development and building", increasingly the ideal of actively embracing sustainable development is being given shape and form, through persuasion, policy, regulation, legislation and now through contract. There is considerable agreement among employers, developers, building technologists, funders, institutions, government and analysts that environmental sustainability is making and will make a very real impact on how clients and the corporate world procure buildings and view the construction process, and how business is audited. Higher energy and material prices are affecting our everyday lives in commerce, in industry and in our homes. We need to adopt the fairest and safest way to protect ourselves against the effects of insecure and costly high carbon energy supplies and catastrophic climate change.

64. The period ahead, I believe, is going to be less about fixed goals per se, although the Climate Change Act here will be a huge catalyst to change, than about innovation and entrepreneurial solutions to what we build or refurbish, and we will begin to see more prescription in our contracts to see this happen, as clients understand more and their consultants lead them down the Path of "Righteousness".

65. However, not all Europe is mad keen on the ideals in practice. Indeed, as the science of climate change gets increasingly urgent, the will of Europe's political leaders to act on the climate crisis seems to be weakening by the day, judging by the EU's package[29] on climate change following months of tough negotiations in the 27-nation bloc. The EU climate package was meant to herald a new and unprecedented level of ambition in tackling climate change. Compared with what the science dictates, we are still way off the mark. There are "destructive forces" within the EU representing their own country's self-interests at the expense of an EU-wide deal. Italy used the current economic crisis as an excuse to stick with its preferred option of continuing with what is, to all intents and purposes, a business-as-usual approach. Poland, with its heavy reliance on coal, fought and won exemption from incurring the full financial cost of burning coal until 2020. Most surprising though, was the extent to which Germany seems to have been instrumental in watering down this package, driven, it would seem, by a heavy lobbying effort from German power utilities RWE and EON, both of which are keen to build new coal-fired power stations, not just in Germany but in the UK too.

66. Business being what it is there is an increasing concern that even the best-intentioned and professionally run corporate-responsibility initiatives cannot deliver sustainable development on the scale needed without the long arm of the law; no one wants "greenwashing". What is needed is the wide recognition that what we do has an effect; doing nothing or too little is not an option[30] - more carrot than stick. Who knows? Those in this theatre will see some big changes! Even if global warming is a myth – doing things this way will be worth all the effort in the long term.

29. The EU package builds on the international commitments made under the 1997 Kyoto Protocol. These commitments only run until 2012, so a UN conference will take place in Copenhagen in December 2009 to map out new targets for the post-Kyoto world. EU governments want other major polluters worldwide to adopt targets similar to the EU's - especially the US, the biggest polluter.

30. Not unlike the butterfly effect, which encapsulates the more technical notion of sensitive dependence on initial conditions in chaos theory and non-linear behaviour. Small variations of the initial condition of a dynamical system may produce large variations in the long-term behaviour of the system.

An update on payment law under construction contracts juxtaposed to the changes in 2009

67. Even though the construction industry has generally reacted favourably to the HGCR Act, there has been unease amongst some that it does not go far enough to protect smaller companies and suppliers. Many believe that the payment and notice provisions are too complex and that adjudication is not always sufficiently accessible. The traditional alternatives of litigation or arbitration are infamously costly and time-consuming.

68. The Government has said the reason for the Bill was that:

> *"Extensive consultation with the construction industry has identified that while the Construction Act has improved cash flow and dispute resolution under construction contracts it is ineffective in certain key regards."*

69. The key policy objectives are to improve the existing regulatory framework in order to:

    (i) Increase transparency and clarity in the exchange of information relating to payments to enable the better management of cash flow;

    (ii) Encourage the parties to resolve disputes by adjudication, where it is appropriate, rather than by resorting to more costly and time-consuming solutions such as litigation; and

    (iii) Improve the right to suspend performance under the contract.

70. The Government commenced consultations on the Act in 2005. The Department for Business, Enterprise & Regulatory Reform (BERR)[31] and the Welsh Assembly Government jointly published the analysis of responses to the 2007 Consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and Scheme for Construction Contracts (England and Wales) Regulations 1998 which led to the Bill published in July 2009 and amended in December as the Local Democracy, Economic Development and Construction (LDEDC) Bill setting out proposed amendments to the Act. The Bill has now passed through the House of Lords (The Bill completed its Lords stages on 29 April 2010 and Lord Tope captured the views of a much wider audience when he summed up the House of Lords' view of the LDEDC Bill 2008:

> "We think that some of it is unnecessary, some of it is undesirable and much of it is well intentioned; there is also some of it with which we simply disagree. The one point on which I think we will all agree is that it leaves this House in a very much better condition than it arrived, but not yet in a pristine condition."

71. It is now in for consideration by the House of Commons and debated at Second Reading on 1 June. The Bill was sent to a Public Bill Committee that completed its consideration of the Bill on 18 June. The Bill will be reprinted before coming back to the House of Commons for its remaining stages on 13 October 2009.

72. Therefore it is now in its final stages of going through Parliament with the Report Stage and Third Reading to go before Royal Assent.

73. However, the Government has indicated that there may need to be further consultations, so it is hard to say with any certainty when the changes will become law and delegated legislation published.

74. The draft Construction Contract Bill proposes the following:

31. But common to this Government's proclivity to change the label on the tin like some change their underwear, on 5 June 2009 the Government created a new Department for Business, Innovation and Skills (BIS). The Department was created by merging BERR (created in June 2007, from the DTI) and the Department for Innovation, Universities and Skills (DIUS).

Contracts in writing

75. The removal of the requirement that for the purposes of the HGCRA contracts had to be in writing or evidenced in writing remains. This means that adjudication will apply to all construction contracts which are either agreed in writing or orally.

76. The Government has put forward two main reasons for this. The first is in order to encourage parties to resolve disputes by adjudication. Thus the Government has acknowledged the difficulties caused by the Court of Appeal decision in the RJT case as noted by, amongst others, HHJ Wilcox who in the case of Bennett (Electrical) Services Ltd v Inviron Ltd [2007] EWHC 49 (TCC) decided that a letter of intent failed to comply with the requirements of section 107. In commenting on the difference of opinion of the Court of Appeal in the RJT case he noted that:

> *The reasoning of Auld LJ is attractive because at the subcontractor level and where cash flow difficulties are likely to be encountered in the smaller projects, the paperwork is rarely comprehensive. The extent of the requirement for recording contractual terms for an agreement to qualify under section 107 laid down by majority could have the effect of excluding from the scheme a significant number of those whom the Act was perhaps intended to assist.*

77. Second, the government noted that it has become common practice to challenge an adjudicator's jurisdiction on the basis that not all the contract was in writing, something which served to frustrate the adjudication. Removing the effect of the RJT decision should put a stop to that. The new proposals are intended to limit the number who are excluded from the right to adjudicate by ensuring the right to adjudicate applies to contracts which are oral or partly oral and not just those which are evidenced in writing. If this makes it through, expect the volume of adjudications to increase at least 10% beyond current levels.

78. The draft Bill in July 2008 had included a new clause 115A, which noted that any contractual provisions relating to adjudication must be "in writing" as defined by that section. This proposed new section no longer appears.

Adjudication costs

79. The draft Construction Contracts Bill had set out certain controls on adjudication costs. The intent remains, but there have been some changes to the previous proposals. The new clause, section 108A, still makes it clear that any attempt to allocate the costs of adjudication (including the costs of the adjudicator) between the parties, will be invalid unless that agreement is made in writing. However, instead of the relevant date of that agreement being "after the adjudicator is appointed", it is now "after the giving of notice of intention to refer".

80. Under the draft July 2008 Bill, the adjudicator had been given a new power, by virtue of section 108B, to determine that any agreed allocation, made in accordance with section 108A, of any part of the costs which a party is required to pay was unreasonable. That idea has not been retained.

81. Finally, the express proposal made in July by virtue of section 108C that parties are jointly and severally liable to pay an adjudicator's reasonable fees and expenses has not been pursued.

Adjudicator's power to make corrections

82. The draft July Bill included a new clause which had the effect of requiring the parties to a construction contract which was subject to Scottish law, to provide in their contract that the adjudicator has the power to correct a clerical or typographical error in his decision arising by accident or omission. The provision concerned must

be in writing. The draft July Bill did not extend that provision to England and Wales as the judgment in Bloor Construction (UK) Limited v Bowmer & Kirkland (London) Limited [2000] B.L.R 314 meant that adjudicators here already have the power to correct mistakes in their decisions.

83. The new Bill makes no such distinction. As had been noted by many commentators, in theory, it would have been open to the appellate courts to overturn the Bloor decision.

Interim payment decisions

84. Under section 109 of the HGCRA contractors are entitled to periodic payments. Concern had been expressed about clauses which make specific payments subject to "interim payment provisions". A new clause was introduced by the July 2008 Bill to render ineffective any contractual provision which provided that a decision taken by a third party as to the amount of any periodic payment is "binding". This has not been pursued.

Withholding notices

85. Despite the criticisms of the drafting of the July 2008 draft [Bill?], the basic scheme in relation to the amendments to sections 110 and 111 remains.

86. The old payment and withholding notice system has been abandoned and is to be replaced with a new payment structure. Given the government's stated aim of achieving an increase in transparency and clarity, this was not surprising.

87. However, a question remains as to whether the new scheme is actually any simpler. The new system, as per section 110A, requires "payment notices" to set out the sum the payer considers to be due and the basis upon which that sum is calculated. It also provides for "payee notices", under section 110B, which can be given in default of the payment notice. If the payer does nothing, the payee can serve their own "payee notice" which will set out the sum the payee considers to be due and the basis upon which that sum has been calculated.

88. The proposed changes would allow a contractor to issue his own default payment notice if the payer Employer failed to issue one on time. The payer employer would have to pay the amount set out in the default payment notice unless it issued a later withholding notice. In some circumstances, an earlier payment application made by the contractor would serve as a default payment notice. In other words, the tables might turn if the employer fails to comply.

89. The sum set out in the "payment notice" or the "payee notice" will become the "notified sum". And a party can only withhold payment from the notified sum in accordance with the new section 111. This new section 111 states that the payer must pay the notified sum unless the payee is given a notice of the payer's intention to pay less than the notified sum. That notice must specify the sum the payer considers to be due and the basis upon which that sum has been calculated. This is where the main criticisms of the draft legislation arise. The new scheme is arguably more complex than before, under the 1996 Act.

90. The government says that this fallback provision, which allows the payee to submit a notice, will help to improve communications between the parties and help to crystallise the debate.

91. Although this might not seem new, a paying party is now required to include details of any set-off or abatement in the notice, something which is currently not always thought to be necessary. This should bring an end to the series of cases, for example Rupert Morgan Building Services (LLC) Ltd v David Jervis and Harriet Jervis [2003] EWCA Civ 1563, about the meaning of the "sum due". Payment notices

are seen by the government as an important tool in achieving transparency and in communicating details of payments which are made or are proposed to be made.

92. Given the government's clear message, it is now unlikely for there to be any recourse for a failure to serve a section 111 notice. The requirement to pay the "notified sum" is intended further to facilitate "cash flow" by determining what is provisionally payable. What is properly due and ultimately payable, as a matter of the parties' contract, is of course unaffected.

93. The new section 111 at subsection (10) makes reference to the House of Lords' decision in Melville Dundas Limited (in receivership) and Others v George Wimpey UK Limited and Others [2007] UKHL 18. Here the House of Lords decided that the payer could legitimately withhold monies, notwithstanding that no "withholding notice" under current section 111 of the HGCRA had been given.

94. The reason was because the contract had provided that moneys need not be paid in the event of the payee's insolvency. As the insolvency had occurred after the period for giving a "withholding notice" had expired, it was simply not possible for the payer to have given such a notice beforehand.

95. Subsection 10 confirms that the Melville Dundas decision remains but is confined to insolvency situations alone.

96. Failures to comply with the existing legislation can have unforeseen consequences for the unsuspecting. Those consequences are likely to be more severe once the proposed changes become law. All personnel responsible for assessing and processing payments will need to be made aware of the protection given by the changes to the Act.

Conditional payment clauses

97. The new subsection 1A, in section 110, which extended the ban on pay-when-paid clauses remains. The ban includes requirements which make payment conditional:

    (i) on the performance of obligations under another contract, or

    (ii) a decision by any person as to whether obligations under another contract have been performed.

The right to suspend

98. The right to suspend work on non-payment is [not often] [seldom] used, because it is such a harsh step. As it currently stands, the Act only gives the right to stop all work. The changes would allow a contractor to stop only part_of the work. That might be a far more powerful weapon, because it means the contractor can focus suspension on a particular area of work, without having to stand down his subcontractors and supply chain members. There would also be a new right to recover all reasonable costs and expenses incurred as a result of stopping work.

99. The unsympathetic problem with the right to suspend under section 112 of the HGCRA is that, in the event of a legitimate suspension, the compensation to which the suspending party is entitled under the legislation is not generous. The suspending party was merely entitled to an extension of time for completion of the works covering the period during which performance is suspended. That extension would not necessarily extend to the seven-day notice period prior to the right to suspend becoming operative, nor would it apply to the time it takes to re-mobilise following the suspension. This is significant since the right to suspend ceases on payment of the amount "due" in full.

100. There is nothing to prevent the parties from conferring more extensive rights through the terms of the contract than the legislation provides. By way of example, clauses 25.4.17 and 26.2.9 of the JCT With Contractor's Design '98 entitle the contractor to apply for extensions of time in respect of "delay arising from a suspension" and "loss and expense where appropriate, provided the suspension was not frivolous or vexatious". Ditto suspension by the contractor under JCT 05, clause 2.29.5 gives this as a relevant event re suspension under clause 4.14[32] of the performance of his obligations under this contract. However, there was nothing to insist that the parties did this. The new draft section 112(3A) introduced in July has been retained. This clarifies the previous problem by making the defaulting payer liable to pay the suspending party "a reasonable amount in respect of costs and expenses reasonably incurred" as a result of suspending.

101. This should help the government to achieve its aim of making the right to suspend performance a more effective remedy.

Current state of the draft Bill

102. One of the documents that were published at the same time as the draft bill was an Impact Assessment ("IA"). This includes some interesting comments about the adjudication process. In discussion upon providing adjudicators with immunity from third-party claims (something which was considered not to be necessary), the IA notes that an average of four complaints about adjudicators are upheld each year. The IA also talks in terms of there being 1,940 adjudications per year. This is a slightly higher figure than the research at Caledonian University currently suggests. It also suggests that if an adjudicator's independence provision was applied, on average an adjudicator would fail the independence test on 5% of occasions. This seems to be a surprisingly high figure. As with most of these IAs one has to be circumspect about the input source and the reasoning by the civil servants!

103. The IA also talks about the small firms' impact test the government carried out and notes in particular that there has been strong support by representatives of small firms for these proposed changes. Indeed, the IA concludes by stressing the benefits of the proposed amendments to small businesses. These include:

   (i) increasing access to a simple mechanism for resolving disputes;

   (ii) improving communication between payer and payee on what will be paid and when;

   (iii) encouraging prompt administration and communication of payment and improving the efficiency and productivity in the industry; and

   (iv) enabling the parties to continue to work together effectively to deliver high quality construction projects on time and on budget.

104. These are areas which should be of benefit to the construction industry across the board, something the government has perhaps missed in its focus on the smaller company. Of course, whether the legislation will achieve these goals is another matter entirely. Certainly a question mark must remain in place about the proposed payment proceedings and it will be important that everyone concerned with payment issues, fully understands what these new changes mean.

Some recent adjudication cases on payment

Withholding notices

105. A party that doesn't want to pay another needs to issue a withholding notice with a reason why it's not paying – but does this reason need to be reasonable?

32. Without affecting any other rights and remedies of the Contractor, if the Employer, subject to any notice issued pursuant to clause 4.13.4, fails to pay the Contractor in full (including any VAT properly chargeable in respect of such payment) by the final date for payment as required by these Conditions and such failure continues for 7 days after the Contractor has given to the Employer, with a copy to the Architect/Contract Administrator, written notice of his intention to suspend the performance of his obligations under this Contract and the ground or grounds on which it is intended to suspend performance, then the Contractor may suspend such performance until payment in full occurs.

106. In *Windglass Windows Ltd v Capital Skyline Construction Ltd & Anr,*[33] Capital engaged Windglass to supply and install windows. The subcontract did not contain an adequate mechanism, in accordance with the HGCRA, for determining what payments were due and when. Accordingly, the relevant provisions of the Scheme were implied into the subcontract. A dispute arose between the parties concerning unpaid interim valuations. Capital, who had only replied to these valuations on two occasions, said that they would not process the applications because they were not in the appropriate format and had not been signed by Capital's site manager. The withholding notices were in the following form:

> *Our financial director has returned this application and is not willing to process this amount due to insufficient supporting information. Please note that our company policy is such that each subcontractor valuation must be presented in a standard format, copy attached, and authorised by the appropriate site manager before your application can be processed. Could you kindly re-present your application with the correct supporting information.*

107. Windglass referred the dispute to adjudication, where they were awarded £152k. Capital did not pay and Windglass sought to enforce the decision. Capital argued that the adjudicator had exceeded his jurisdiction in deciding that the withholding notices were invalid because they did not include valid grounds for withholding. Capital argued that the HGCRA does not require the grounds for withholding to be valid for the notice to be [effective] [elective]. Mr Justice Coulson held that Capital were wrong for four reasons:

   (i) In deciding that the notices were invalid, and that any cross-claims raised as defences to the notices must fail as a consequence, the adjudicator had answered the issues put to him. This was within his jurisdiction and the Judge queried whether this was a jurisdictional point in any event;

   (ii) The argument that the HGCRA did not require the grounds for withholding to be valid was wrong. The Judge disagreed that, as long as there was something which purports to be a withholding notice, then that is sufficient to justify withholding, regardless of content. There was no meaningful distinction between a 'valid' and an 'effective' notice in s111;

   (iii) The adjudicator provided reasons as to why the withholding notices were not effective: neither the amount proposed to be withheld nor the grounds for doing so were set out; and

   (iv) Even if the adjudicator should have taken the alleged counterclaim into account, it was so vague, unparticularised and unlinked to the terms of the subcontract that it could not operate as a valid set-off to the withholding notices.

108. Capital also submitted that their withholding notices could act as a 'gateway' through which they could gain an entitlement to raise defences in the adjudication not previously raised. The Judge disagreed on the basis that the HGCRA does not permit someone to put in an ineffective withholding notice to get around the requirements of the HGCRA, and to then introduce entirely different arguments at a later date. The decision was duly enforced.

109. As a comment, there will be many adjudicators' sympathetic to the subcontractor, who has not been provided in a withholding notice with any evidence of loss resulting from a purported delay and who argues therefore that the notice is not valid and the sum deducted must be paid. It thinks that the argument is so strong that it does not bother making a case that it did not cause delay - it relies on the want for detail in the withholding notice. However, adjudicators cannot assist. A notice that states the sum to be withheld and the ground for withholding is a valid notice. The "ground" can be manifestly wrong, but that does not stop it from being

33. [2009] EWHC 2022(TCC)

a ground and so fulfilling the requirements of the Act. If money is being deducted because the subcontractor's supervisor drove a red car, so be it. That is unlikely to be a good contractual argument, but it is a valid notice of withholding. To challenge it, the subcontractor must argue that red car has no contractual significance, that the supervisor cannot drive, and if he was the main contractor has not suffered any loss!

Can an adjudicator's decision be setoff against an arbitrator's award?

110. In *Workspace Management Ltd v YJL London Ltd*[34] the court found that it was "clear beyond doubt" that the adjudicator had found that the contractor had overpaid the employer. This could be seen from the adjudicator's decision (which set out the precise amount overpaid) and his letter of 6 January 2009.

111. Although the adjudicator's decision did not direct the employer to repay the overpayment to the contractor, the court found that:

> *the Adjudicator's decision means that, as a result of the inexorable logic of his valuation, the Claimant [the employer] has been overpaid by the Defendant [the contractor] ... either the Adjudicator's decision that the sum was due to the Defendant is express, or it is to be reasonably inferred from the inevitable and logical consequences of his valuation. (Paragraph 19, judgment)*

112. In reaching this conclusion, the court referred to two previous TCC judgments on what can be inferred from an adjudicator's decision, *David McLean Housing Ltd v Swansea Housing Association Ltd [2002] BLR 125* and *Balfour Beatty Construction v Serco Ltd [2004] EWHC 3336 (TCC)*.

113. Although an adjudicator did not require the repayment of a sum overpaid, in finding that there had been an overpayment, *the requirement followed logically by reasonable inference*, if not express. The argument that the adjudicator had no jurisdiction to consider whether an overpayment had been made failed. Although the reference was to consider sums claimed by claimant from defendant, the adjudicator was not required to stop his valuation without reaching a final result. The defendant was entitled to use the sum overpaid as a set-off against an arbitration award against it because it was not a mere counterclaim but a decision binding on the claimant.

114. However, it seems that *a party cannot withhold payment against an adjudicator's award by virtue of cross-claims and set-offs if he issues a notice of intention to withhold payment* ***after*** *the award is issued*. Per: VH*E Construction Plc v RBSTB Trust Co Ltd;*[35] *Solland International Ltd v Daraydan Holdings Ltd;*[36] *Construction Group Centre v Highland Council,*[37] affirmed. See too: *Balfour Beatty Construction v Serco*[38] *- Section 111 of the HGCR Act does not apply to payments due in consequence of an adjudicator's decision.*

115. Further, a contract term which seeks to override the statutory obligation to comply with the adjudicator's award will not be effective: see *Ferson Contractors v Levolux,*[39] disapproving *Bovis Lend Lease Ltd v Triangle Development Ltd*[40] and, it seems, *KNS v Sindall,*[41] cf. *David McLean Housing Contractors v Swansea Housing Association,*[42] where the sum found payable by the adjudicator was incorporated into a certificate against which the employer issued an effective notice of intention to withhold payment.

116. If, on a proper construction, the adjudicator's decision is as to a sum which will become due *in the* ***future***, as opposed to a sum already due, then a withholding notice may be served validly *providing the sum awarded has not in the meantime become due*. Per *Shimizu Europe Ltd v LBJ Fabrications Ltd*[43] considered in *Severability of Adjudicator's Decisions* by Sheridan and Helps (2004) 20 Const. L.J. 71.

34 [2009] EWHC 2017 TCC
35 [2000] BLR 187
36 (2002) 83 Con. L.R. 109
37 [2002] BLR 476
38 [2005] CILL 2232
39 [2003] BLR 118
40 [2003] BLR 31
41 [2000] 75 Con. L.R. 71.
42 [2002] BLR 125
43 [2003] BLR 381

117. We move next to the latest on set-off of adjudicator's decisions - *HS Works Ltd v Enterprise Managed Services Ltd*[44] - and the difficult situation that arises when there are two enforceable adjudication decisions which decide different things but which may spark off each other.

118. The subcontractor performed repair, reinstatement and resurfacing works for the contractor. Following completion of the works a dispute arose between the parties as to the valuation of the final account and the level of a number of contra-charges. Two adjudications followed.

119. In the first adjudication brought by the subcontractor, the adjudicator decided that £1.8m deducted by the contractor as contra-charges should be awarded to the subcontractor.

120. In the second adjudication, the adjudicator decided that the proper valuation of the subcontractor's works was £24.81 million (less the value of the contra-charges of £1.56 million), leaving the final valuation of the subcontractor's works as £23.25 million. The effect of the second adjudication was that all or part of the sum awarded to the subcontractor in the first adjudication should be repaid.

121. The contractor and the subcontractor both argued that the decision where they had lost was invalid. The applications to enforce those decisions were joined together before Mr Justice Akenhead.

122. The court had to address how the court should give effect to the two adjudication decisions and, in particular, whether one could be set off against the other.

123. The starting point was that the court should follow the general principle that adjudicators' decisions generally should be enforced promptly, unless there were special circumstances. The existence of a subsequent decision was not generally a special circumstance that justified departing from the general rule (*YCMS Limited v Grabiner*[45]).

124. Mr Justice Akenhead then presented the following guidance as to whether the court could set off one decision against another:

- First, it was necessary to determine whether both decisions were valid.
- Provided both decisions were valid, it was necessary to consider if both were capable of being enforced or given effect to; if one or other was not so capable, the question of set-off did not arise.
- If it was clear that both decisions were capable of being enforced, the court should give effect to them both, provided that separate proceedings have been brought by each party to enforce each decision. The court had no reason to favour one side or the other if each had a valid and enforceable decision in its favour.
- It was a matter for the court how each decision would be enforced. It might be wholly inappropriate to permit a set-off of a second (financial) adjudicator's decision in circumstances where the first decision was predicated on the basis that there could be no set-off.

125. The court also considered the approach that should be taken to what has been called "kitchen sink" adjudications - disputes which are so extensive that the adjudicator or the defending party could not readily or easily deal with them in the standard 28-day period of adjudication.

126. Mr Justice Akenhead was of the view that the court should have regard to:

[44] [2009] EWHC 729 (TCC)

[45] [2009] EWHC 127 (TCC)

- whether and upon what basis the adjudicator felt able to reach his decision in the time available;
- the opportunities available to the defending party before the start of the adjudication to address the subject matter of the adjudication; and
- whether the defending party was able to and did address the material provided to it and the adjudicator.

127. The subcontractor argued that the contractor had failed to issue a valid withholding notice in respect of the contra-charges as was required by the contract and so had no contractual or lawful right to withhold the sum of £1.8 million.

128. The contractor argued that the adjudicator should have considered the merits and quantum of the contra-charges which it had put forward, as opposed to the "artificially narrow grounds" of whether a withholding notice had been issued, and that in failing to address the contra-charges claim, the adjudicator had failed to follow the rules of natural justice.

129. The adjudicator decided that as a valid withholding notice had not been issued in time the effect was that no sums could be withheld from the amount due to the subcontractor.

130. In reviewing the decision of the adjudicator, the court was satisfied that the adjudicator's decision was valid. In reaching his decision on the subcontractor's primary case that there was no effective withholding notice, there was no need for the adjudicator to consider whether the contra-charges claim was a good or bad claim.

131. The contractor had sought a declaration as to the proper valuation of the works carried out by the subcontractor. The subcontractor argued that the adjudicator had no jurisdiction because the adjudicator had failed to act fairly or apply the rules of natural justice by continuing to issue his decision despite the late provision of the contractor's expert witness report and the extent of the adjudication (38 lever arch files, a number of smaller files and three compact disks of data).

132. In reviewing the decision of the adjudicator, the court was satisfied that the adjudicator's decision was valid. The court noted that it was clear that the adjudicator did not consider that he needed more time to produce his decision although he had acknowledged that his task had been onerous. There had been no hint or suggestion that the adjudicator thought that he could not act fairly in producing his decision. The adjudicator had done a thorough and conscientious job and the adjudicator's approach could not be criticised.

133. The decisions in the first adjudication and the second adjudication were both valid and enforceable.

134. The court took into account the fact that both decisions should have been complied with when the decisions had first been issued. The fact that the parties had not done so had left the court in a difficult position as to how to deal with what had happened.

135. The court had a discretion as to how to give effect to the decisions in the two adjudications, and, on balance, considered that the court's order should reflect the net effect of the decisions.

136. Mr Justice Akenhead took a pragmatic approach to the issue on the basis that "it would be pointless, at least administratively" for the contractor to hand over the sum awarded in the first adjudication, to be followed by the subcontractor having to hand back all or the bulk of what had just been paid to it by the contractor.

137. This case provides useful guidance on the principles that the court will adopt when considering simultaneous enforcement of adjudicators' decisions. The court exercised its discretion pragmatically and made an order to reflect the net position of the parties.

138. The court also confirmed the views set out in *CIB Properties v Birse Construction*[46] and in *Dorchester Hotel v Vivid Interiors*[47] that in "kitchen sink" adjudications, it is for the adjudicator to decide whether or not he can reach a decision fairly within the timetable. If the adjudicator is of that view the court generally will not intervene except in the most obvious case.

[46] [2005] 1 WLR 2252

[47] [2009] EWHC 70 (TCC)

Summary of the JCT 2009 revisions[48] to payment etc.

139. The JCT[49] (more than 70 % of all projects in the UK are built under a JCT contract) summarises the changes to the contracts as follows:

> *The principal revisions are the incorporation of sustainability provisions, following the JCT's consultation, and the provisions building on OGC's Achieving Excellence Criteria. The opportunity has also been taken to modify aspects of the payment provisions, while awaiting the outcome of the proposed payment legislation.*

140. Further aspect was given at the JCT's launch event for the 2009 revisions, on 18 May 2009. Two particular changes were highlighted:

- Changes to the payment provisions. Applications for interim payment are now made every two months between practical completion and the end of the rectification period or issue of the notice of completion of making good (whichever is later). (See, for example, clause 4.9 of JCT DB05, Revision 2 2009.)

- New requirements for complying with the Achieving Excellence in Construction initiative.[50] Provisions in line with the Office of Government Commerce's (OGC) Achieving Excellence in Construction initiative are included in the 2009 revisions by default, unless the parties indicate otherwise in the JCT Contract Particulars. (See, for example, Schedule 9 to the JCT SBC05, Revision 2 2009.)

141. The principal amendments to the JCT DB (Design and Build) form are contained in Part 2 of Schedule 2 (Supplemental Provisions) and include:

- A mechanism for the Employer to instruct the acceleration of the Works with the agreement of the Contractor.

- An obligation on the parties to work in a co-operative and collaborative manner, in good faith and in the spirit of trust and respect.

- An extension of the health and safety provisions already included in the body of the JCT form.

- A mechanism for the Contractor to propose value engineering changes to reduce the cost of the Works, their associated life-cycle cost, and to improve generally the environmental performance of the Works.

- A mechanism for the incorporation by the Employer of key indicators to measure the Contractor's performance.

- An obligation for the early notification of disputes and for senior executives to engage in good faith negotiations to resolve such disputes.

142. Unfortunately, while the JCT guides to the individual contracts (where these are published) will identify the clauses that have changed, no list of individual amendments will, it seems, be published. Users who, for example, amend or advise on the detail of JCT clauses will be required to carry out a line-by-line assessment of the changes.

143. According to JCT, the 2009 revisions provide the opportunity to adapt certain aspects of the payment provisions, whilst awaiting the outcome of the proposed new payment legislation referred to above to repeal the Housing Grants, Construction and Regeneration Act.

144. I take with a pinch of salt the contention the changes embrace OGC's Achieving Excellence criteria, so that JCT can become the contracts of choice across government departments, as I have to admit to a certain cynicism in the OGC's

48. Note, too, that the changes mean termination for contractor default has increased notice period from 14 days to 21 days is now required in the case of Contractor default and the mediation provisions - each party to give "serious consideration" to any request to refer a matter to mediation. [check for sense]

49. Sweet & Maxwell Thomson Reuters.

50. It sounds unctuous but the aim through the Achieving Excellence in Construction initiative is for central government departments and public sector organisations to commit to maximising, by continuous improvement, the efficiency, effectiveness and value for money of their procurement of new works, maintenance and refurbishment. The National Audit Office (NAO) report, Improving Public Services Through Better Construction, published in March 2005, highlighted that an £800 million overspend on construction projects had been avoided through the adoption of the AEC best practice principles.

The same report estimates that further value gains of up to £2.6 billion in annual construction expenditure are possible if good practice was applied across all the public sector.

ability to judge what is best given their ringing endorsement of the NEC on a basis later shown to be based on not knowing the alternatives!

145. Following the format first introduced for Revision 1, JCT have continued the policy of listing the changes in the Contract Guide rather than the contract itself. The guide also now includes, at Appendix C a "user checklist" with tick boxes of "key information" that will assist completion of the Articles of Agreement. It is not clear whether JCT intends that a separate checklist – and therefore guide – is needed for each new project.

146. There will be some amendments which relate to specific contracts, and not all revisions apply to all documents, but the broad changes are as follows:

Conditions:

- Changes to the notice provisions including period required before terminating increased notice period from 14 days to 21 days is now required in the case of contractor default
- Acknowledgement of the use of a framework agreement
- Requirements for collaborative working
- Provisions for establishing and monitoring of contractor's performance against indicators identified in the contract documents.

Payment:

- A new provision for interim payments after practical completion at intervals of two months
- Clarification of the dates from which interest is calculated where payment is made late
- The option of a retention bond in lieu of retention, together with sample text
- The option of an Acceleration Quotation to be submitted by the contractor.

Dispute resolution:

- Parties must "give serious consideration" to any request to refer disputes to mediation
- Meetings between senior executives may be arranged to negotiate in respect of any disputes
- Encouragement to agree a communications protocol at the outset.

Sustainability:

- The contractor is encouraged to propose changes to designs or specifications or programmes which may benefit the employer in terms of cost of works or life cycle cost
- The contractor is encouraged to suggest economically viable amendments to the works which may result in an improvement in environmental performance
- Parties shall work with each other in a collaborative and cooperative manner.

Comment

147. The decision to withdraw JCT Revision 1 (or other earlier versions) from bookshops and not to publish stand-alone sheets of amendments has come in for some stick, particularly in the current economic climate.

148. Given the expected changes to the statutory landscape for construction projects, the decision to amend the JCT's payment clauses may also be questioned by some for jumping the gun. However, given the nature of statutory and voluntary regulation affecting the long-term sustainability of construction projects, any steps that can help unify sustainability procedures for the industry can only be a good thing.

149. It is uncertain whether the 2009 revisions will secure the JCT against the mounting popularity of other standard forms of contract, such as the NEC3 suite of contracts, but let's not lose sight of the fact that JCT still mops the floor with NEC in terms of volume of use in the UK. The 2009 revisions demonstrate a continuing commitment to meeting the changing needs of the construction industry (particularly in relation to environmental sustainability).

Common legal myths with JCT on "snagging"

"Snagging"

150. Building works, like the arrow of Eleatic paradox, have a propensity to get closer and closer to completion but never quite to arrive. The building industry accordingly has evolved the concept of practical completion.[51] The term is widely understood in the industry as meaning the stage at which the works are reasonably ready for their intended use, notwithstanding that there may be outstanding "snagging" items.

151. There is a fairly widespread misconception that the defects liability period (now the defects "rectification period" since JCT 05) is intended as a time when the contractor attends to snagging items outstanding as at the date of practical completion and obtains release of the final moiety of retention having done so. In fact, the scheme of the JCT contract is that there should not be any outstanding items at practical completion, and the defects liability period / rectification period is the period in which the parties "wait and see" as to what defects emerge. If we stop here, that is all you really need to know in my opinion!

152. The approach JCT has taken historically is that the defects liability period / defects rectification is akin to a guarantee period and the contractor usually has the obligation, and indeed the right, to remedy defects appearing within this time. The contractor is usually required to remedy these defects free of charge but the practice is to the benefit of both parties since the contractor would otherwise be liable for the greater cost of another contractor remedying the defects.[52]

153. The term "snagging" is more commonly used to describe unsatisfactory work or small items of work still to be completed which are discussed/discovered during final site inspections. It has given birth to a small industry of contractors that specialise in making good, particularly to the order of national house builders! Snagging lists are also termed Schedules of Outstanding Works.

154. As to definition, Peter E.D. Love and Heng Li[53] in *Construction Management and Economics* describe snagging as "an act of rework; the unnecessary effort of re-doing a process or activity that was incorrectly implemented the first time". In house construction it is the process by which an item is made to conform to the original requirement by completion or correction." They go on to refer to a "Snagging Survey" as a detailed inspection report of a newly completed building providing a defect assessment focused on industry-established finishing standards.

Architects' duties to inspect the works and snagging

155. In the following case, the judge observed that the architect's inspection role has been the subject of surprisingly few cases despite the "snagging industry". This case is therefore of particular interest.

156. *Ian McGlinn v Waltham Contractors Limited and others*[54]

The employer was a multi-millionaire who engaged a contractor and professional team to design and construct a house in Jersey. Preferring to keep things "informal and fluid", no formal contract was ever entered into by the employer with either the contractor or the architect. Delays occurred in the construction of the house and the construction cost soared over the original budget. The contractor walked off site and subsequently went into administration. The employer chose to demolish the property in view of the alleged defects and then brought proceedings against various parties, including the architect.

157. The terms of engagement of the architect and, in particular, the scope of services which the architect had agreed to provide, were fiercely disputed. Whilst the employer and architect agreed that the engagement of the architect incorporated

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[51] Under JCT 05, clause 2.30, when in the opinion of the Architect/Contract Administrator practical completion of the Works or a Section is achieved and the Contractor has complied sufficiently with clauses 2.40 and 3.25.3, then:
- 1 in the case of the Works, the Architect/Contract Administrator shall forthwith issue a certificate to that effect ("the Practical Completion Certificate");
- 2 in the case of a Section, he shall forthwith issue a certificate of practical completion of that Section (a "Section Completion Certificate");

and practical completion of the Works or the Section shall be deemed for all the purposes of this Contract to have taken place on the date stated in that certificate.

[52] Contrast NEC/EEC where the defects correction period with the ECC is usually a short period of between two to four weeks. This means that when a defect is notified to the Contractor he is expected to correct the defect within the stated period. Whilst it is also true that the defects period is also given (usually between six and eighteen months) this does not allow the Contractor simply to put right the defects at the end of that period but is rather a longstop period within which defects are to be notified and corrected within the shorter period for defects correction starting from the date of notification. This has the potential for the Contractor to be in breach of contract for failure to correct the defect within the sated period even though he has been unable to obtain access to the site to correct the defect.

[53] Construction Management and Economics, 1466-433X, Volume 18, Issue 4, 2000, Pages 479-490.

[54] [2007] EWHC 149 (TCC)

the "Architect's Appointment" document published by the RIBA in 1982 (sometimes known as the Blue Book), the extent to which this document was incorporated was disputed.

158. One of the breaches of contract claimed against the architect related to its failure to inspect the works. Under the "Architect's Appointment" document, the architect's obligation was to visit the site as appropriate to inspect generally the progress and quality of the work.

159. Before considering whether the architect had complied with its contractual obligation to carry out inspections to identify non-compliant work, the judge reviewed the authorities and set out the following legal principles applicable to the "inspecting professional" (for convenience, I refer below to the "inspecting professional" as "the architect"):

Legal principles in relation to an architect's duty to inspect

160. The legal principles derived by the judge from the authorities were:

- The frequency and duration of inspections should be tailored to the nature of the works going on at the site from time to time.
- It was not enough for the architect to carry out inspections on the date of each site meeting (whether fortnightly or monthly) but not otherwise. The dates of such site meetings might have been arranged some time in advance, without any reference to the particular elements of the works being progressed on site at the time. Moreover, if the contractor knew that inspections were confined to the dates of the site meetings, it would know that, at all other times, its works would be safe from inspection.
- Although the architect could instruct the contractor not to cover up important elements/stages of the works until they had been inspected, this situation was unlikely to arise in most cases. This was because an architect carrying out inspections tailored to the nature of the works proceeding on site would have timed its inspections so as to avoid such inspections affecting the progress of the works.
- In any claim against an architect for an alleged failure by it to carry out the proper inspections, the mere fact that defective work had been carried out and covered up between inspections would not automatically give an architect a defence.
- Matters such as the architect's reasonable contemplation of what was being carried out at the site at the time, the importance of the element of work in question, and the architect's confidence in the contractor's overall competence would determine whether or not such defence would apply.
- If an element of work was important because it was going to be repeated throughout one significant part of the building, then the architect should ensure that it saw that element of the works in the early course of construction/assembly, so as to form a view as to the contractor's ability to carry out that particular task.
- Reasonable examination of the works did not require the architect to go into every matter in detail: it was almost inevitable that some defects would escape its notice.
- It was misconceived to assume that, because the employer had a claim for bad workmanship against the contractor, the architect must have been negligent or in breach of contract for missing the defect during construction.

The architect did not guarantee that its inspection would reveal or prevent all defective work.

Were monthly inspections, on the days of site visits, adequate?

161. During the critical period of construction - of the main structure of the house - the inspections were carried out monthly, on the same day as the monthly site meeting, and not otherwise. There was no evidence to suggest that the inspections were arranged at a time that was suitable for the particular progress of the works on site.

162. The judge held that such monthly visits, telegraphed in advance, were too rigid and too inflexible. The architect had not performed its inspection function adequately. The judge also criticised the complete absence of any records generated by the architect of the defects seen during the inspection and the remedial action required by the architect.

Is an architect entitled to wait until handover before undertaking a detailed inspection and producing a snagging list?

163. This issue was relevant for the following reason. Defects observed needed to be accounted for in the interim payment certificates. If defects had not (but should have) been accounted for in interim certificates, then if (as here) the construction contract came to a premature end, it would be difficult for the architect to avoid responsibility for any consequent overpayment where (as here) this could not be recovered from the contractor.

164. The judge's view was that the answer to the question - as to whether an architect was entitled to wait until the contractor's handover of the building before undertaking a careful inspection and producing a detailed snagging list of incomplete/defective work - depended upon the nature of the defect in question.

Two different categories of defects

165. The judge described two different categories of defects which may be revealed during an inspection prior to handover:

- Defects which must sensibly be remedied at the time, rather than at the end of the project. If the architect identified such defective work, then the architect was obliged to point this out to the contractor and to require the defective work to be rectified.

- Defects in work that was still in the process of being carried out (referred to as "temporary disconformities"). If the architect identified such defects, it was not obliged to point these out. In other words, the architect should only condemn a defect: if the work was not yet finished, it could not fairly be said to be defective.

166. To determine whether the architect was liable for any overpayment to the contractor resulting from payment for defective work (which it was impossible to recover from the contractor, who was in administration), the judge analysed the defects alleged and decided into which of these two categories of defects each alleged defect fell.

How should the employer's losses be quantified?

167. Was the employer entitled to recover damages by reference to:

- the diminution in value of the property;

- the costs of repair; or

- the cost of demolition and rebuilding of the building?

168. The judge accepted that this was unquestionably a case where the correct measure of loss was reinstatement: the critical question was whether the reinstatement costs should be calculated by reference to the costs of demolition and rebuilding (the employer's case); or the lower costs of reinstating the individual defects for which the architect was found liable (together with appropriate additions for on-costs and the like (the architect's case).

The employer's argument: the "Great Ormond Street principle"

169. The employer argued that:

- the decision to demolish the property was taken on expert advice;
- it was not suggested that such advice was negligent; and
- the employer was therefore entitled to the costs, or a proportion of the costs of demolition and rebuilding from the architect (and other defendants) in accordance with the "Great Ormond Street principle".

170. The "Great Ormond Street principle" came from a passage in *The Board of Governors of the Hospitals for Sick Children & Anor v McLaughlin & Harvey plc and Ors,*[55] in which Judge Newey said:

- A claimant who carries out either repair or reinstatement of his property must act reasonably.
- A claimant can only recover as damages the cost which the defendant ought reasonably to have foreseen that he would incur. The defendant would not have foreseen unreasonable expenditure.
- Reasonable costs do not, however, mean the minimum amount which, with hindsight, it could be held would have sufficed.
- When the nature of the repairs is such that the claimant can only make them with the assistance of expert advice the defendant should have foreseen that he would take such advice and be influenced by it.

Did the Great Ormond Street principle apply in this case?

171. In the *Great Ormond Street* case, engineer's modifications to the piling design of the new wing of the hospital were negligent and, as a result, the foundations as constructed were inadequate. Remedial works were required: the only issue was whether the engineer could criticise the particular remedial scheme that had been carried out.

172. The circumstances in the *McGlinn* case were significantly different:

- The property was structurally sound - the defects essentially related to aesthetic matters.
- The expert advice in relation to demolition was dependent upon the comparative costs of (i) repair (since the building was structurally sound), and (ii) demolition and rebuilding. Although the expert advice was that the quantum of such figures was reasonably comparable, there was a clear risk that the cost of demolishing and rebuilding (which involved so much more physical work) might increase.
- The expert advice (on which the employer sought to rely) in this case was not only wrong (since the demolition/rebuilding cost turned out to be far greater

55. [1987] 19 Con LR 25

than the agreed repair cost). It was also based on a risk assumption (ignoring the risk that demolition/rebuilding costs might increase) that was (in the judge's words) open to considerable debate.

- The employer had a very real difficulty. Essentially, he relied upon/assumed complete success on, a large number of contentious defects, in claims against four separate defendants. If one significant item was removed from the equation (e.g. because it was not a defect at all), where did that leave the expert's advice to demolish or rebuild? It might not make the advice negligent, but it did fundamentally weaken its evidential value.

The judge's conclusion

173. The judge found that, on the facts of this case, the appropriate measure of damages to be awarded against the architect was the (largely agreed) cost of the repair work necessitated by the individual defects for which the architect was liable.

Comments

174. As the judge observed, to knock down a completed building where the majority of the alleged defects were aesthetic only was, on any view, an extreme course. The so called "Great Ormond Street principle" would not apply in the vastly different circumstances of this - somewhat bizarre - case. Overall, some very sound judicial guidance on the subjects of inspection, snagging, defects and damages, which we can all learn from.

Sectionalisation and time at large

175. It is not uncommon for a project to have two or more completion dates for different parts of the project works, i.e. sectional completions, rather than have one completion date for an entire project. In JCT 05, the Contract Particulars refer to Sectional Completion dates and, if these are inserted within the Particulars, the Contract will operate to give effect to the Parties' intentions. The JCT 05 includes provisions that were previously separate supplements to the main contract. The appendix at the end of the old forms is now at the front, so that all of the project's specific information is clearly placed at the beginning of the contract.

176. If the client has failed to make the sectional completion requirements an express term of the contract, instead only listing them in the bill of quantities or pre-award minutes, with just one main completion date in the contract, difficulties will inevitably arise post-contract.[56] In this instance, it is the date in the contract particulars that is binding - something that has the potential to lead to a major breakdown in client/contractor relationships.

177. The parties may want sectionalisation because a project consists of a number of discrete buildings and an employer wishes to take possession of each of the buildings in a set or logical sequence as they are completed. Or, if an employer wishes to take early possession of the different floors of a building in order to do its own fit-out or comms. works while the contractor continues with the remainder of the works. While this may sound like a perfectly logical arrangement and even reciprocally beneficial, introducing sectional completions profoundly affects a project in several ways.

178. It is important not to lose sight of the fact that sectional completion with multiple completion dates for the different parts of work being undertaken must be made express as contract machinery in contrast to a more traditional set-up where there is a single completion date for an entire development. A sectional completion clause is very important as it is in place for the benefit of the employer. Without it, the contractor maintains the right to possession to occupy the entire site for as long as there is contracted work that requires completion. This poses a major financial risk to the employer. Without the implementation of sectional completion on a major mixed-use development, for example, the client would be unable to take possession of any of the completed retail, and begin to recoup his investment, until all of the works reached practical completion.

179. As a result, sectional issues require special deliberation when a project is being planned and in certain circumstances can cause complications for contractors, should they need to apply for an EOT. The special considerations include the following:

180. Firstly, sectional completions mean that as soon as a sectional completion date is achieved and a part of the works taken over, the contractor will be sharing the site with either the employer, the employer's contractors, the occupier, the occupier's contractors or all of them.

181. This could mean that access and compounds/laydown areas will be shared and checks will need to be made to ensure that they are adequate for the requirements after the sectional completion has been achieved. For example, are the lifts or hoists capable of carrying the additional personnel, materials going in and waste material going out? Will they have to work over and above the usual site working hours?

182. Secondly, the nature of the sectional completion has to be established. Does it mean that a contractor is expected to hand over a section of works for the exclusive use of the employer, or will the contractor have to work alongside others? In which

56. Gleeson Ltd v London Borough of Hillingdon, (1970) 215 E.G. 165, JCT Clauses 2.33 to 2.37 concerning Partial possession by Employer under JCT 05 provide for the Employer with the consent of the Contractor to take possession of part or parts of the Works before the Works are completed, and for the application to each part of provisions for Practical Completion, defects, insurance and liquidated damages analogous to those which apply to the whole. Clauses 2.33 to 2.37 should be read with Clauses 2.30 and 2.38 to 2.39, but it is well settled that this clause does not as such provide for sectional completion.

case responsibility for keeping the section clean, for security, fire risk and insurance needs to be established for the section that has been handed over.

183. Thirdly, while it is easy enough to identify a section of works that can be completed in advance of another section, contractors and employers need to ensure that the part of the project that makes up the sectional completion dates can actually be handed over, i.e. that there are no reliances, be they services, link structures or functional dependencies.

184. The reason for this is that when tender documents are assembled it may not be apparent to an employer and its team that it may not be possible to hand over a section of works exactly as an employer requires it. For example, an archetypal situation that can occur is a floor of a building intended to be part of a sectional completion and handed over to the employer but there happens to be a transformer or UPS through it feeding other floors. This means that the contractor will still need to gain access to the floor that has been handed over and carry out its work. A further situation is that it might be found that a section of works to be handed over is fed with services from another section that is not part of the section to be handed over. Therefore, employers need to make it clear whether and what live services are required for each sectional completion. Similarly, contractors have to ensure that their works are programmed to provide live services if they are required to complete a section, or make it clear that they will not or cannot be made available. No point handing over a control tower on an airport without the telemetry connections made to that control room!

185. In most cases, these situations can be managed with some pre-planning and the sectional completion can be achieved without hindering either the contractor or the employer. However, it requires analysis during the tender stage by the contractor to identify these situations so that any problems can be managed out. The contractor should then describe in its method statement how the sectional completion will be handed over and include a marked-up drawing showing the boundaries of the section, access and egress routes, any limitations and any other information that is relevant.

186. In terms of planning, sectional completions also have a profound effect on a programme. Each sectional completion actually creates a separate critical path for each section, thereby reducing the buffer of float that might otherwise exist if there were a single completion date. This reduces the capability of a programme to absorb delays which affects both a contractor and an employer. For a contractor, if it is in delay in the process of completing work that forms part of a sectional completion it only has the remainder of the duration allowed for the particular section to make good the delay, so opportunity is lost. For an employer it means that if it causes a delay the contractor will probably apply for an EOT to the affected sectional completion date. If, however, there was only one completion date at the end of the works a contractor has a much greater scope and therefore chance of overcoming a delay by mitigation and there may be no delay arising. So sectionalisation is usually priced accordingly by contractors.

187. Sectional completions have the positive effect of forcing contractors to focus on progressive completion and handover of the project, rather than endeavour to hand over the entire project on one day, but sometimes their preoccupation becomes dealing with each section in isolation at the expense of later sections. Further, by having sectional completions a formal structure is set up where an employer takes possession and responsibility of completed sections of work rather than let a contractor take responsibility for the entire works until the last section is completed. Assuming, that is, the employer does not want to take partial possession of part of the works as it is completed.

188. Sectional completions become contentious when there is an employer delay to a sectional completion and it has to be decided what the impact of the delay is on other sectional completions. If there is a clear physical relationship from one sectional completion date to a subsequent sectional completion date there should be little debate (in theory!) that both have been delayed. If there is not a clear physical relationship between two completion dates things are less clear cut. In such circumstances an employer may feel that if it delays a sectional completion date it should have no impact on subsequent sectional completion dates.

189. On the other hand, a contractor will probably feel that while there is no physical relationship between two sectional completions there is a resource link between them, whether it is shown on a programme or not, and to delay one sectional completion will delay resources that were to carry out works for the subsequent sectional completions which will also be delayed.

190. There is no easy way out of this and in these circumstances it is worth an employer and contractor agreeing how EOT issues will be dealt with before they go into contract together. A reasonable employer should accept that a contractor would find it difficult to hand over two sections at the same time, and an approach that can be adopted is to have an agreement that a contractor can absorb say two weeks of employer delay before it impacts on subsequent sectional completions.

So what can contractors do to protect themselves?

191. Prior to submitting a price, a contractor must ensure that the proposed sections are clearly defined and the logic behind the sectional possession and completion dates is viable in relation to the programme for the works. Full consideration must be given to the effect of a delay to one section on the commencement and completion of other sections. Adequate allowances within the tender for the requirement of such interfaces are therefore critical.

Are any other issues likely?

192. Probably the biggest consideration for the client will be the effect of delay in completion of each section when estimating liquidated damages. A provision for liquidated damages will be enforceable if the amount fixed is a genuine pre-estimate of the loss likely to arise from the anticipated breach, judged at the time the contract is entered into. But while the client doesn't need to prove actual losses, liquidated damages are not enforceable if deemed a penalty. Two cases, *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd*[57] and *Philips Hong Kong Ltd v The Attorney General of Hong Kong,*[58] provide some guidelines for distinguishing between liquidated damages and a penalty. In short, it is a penalty if the sum is "extravagant or unconscionable in amount in comparison with the greatest loss which could conceivably be proved to have followed from the breach".

193. In such circumstances, the liquidated damages provision should confirm how the sums payable for delay are apportioned between the different stages of work. A failure to correctly do so can be fatal to any claim for liquidated damages.

194. One of my cases, *Taylor Woodrow Holdings Limited and George Wimpey (Southern) Limited v Barnes & Elliott Limited,*[59] illustrates the importance, when incorporating provisions for Sectional Completion, of defining the Works within each Section. This case related to an appeal under section 69(1) of the Arbitration Act 1996 from a partial award of Eric Mouzer. On the facts of the case, the liquidated damages provisions of a modified JCT contract were void for uncertainty. The date upon which particular sections of the work were to be completed was neither defined nor ascertainable, nor could any sectional work be valued such that time was at large. The Contract took the form of the JCT Standard Form of Building Contract with Contractors Design (1998 edition), incorporating Sectional Completion. The Works converting the former Long Grove hospital to residential units were divided

57. (1915) AC 79
58. (1993) 61 BLR 41
59. [2004] EWHC 3319 (TCC)

into six Sections. The contractual provisions that were relevant to the preliminary issues to be determined were:

"The Conditions of Contract

2.1 The contractor shall, subject to the conditions, carry out and complete by sections the works referred to in the Employers' Requirements, the contractor's proposals (to which the contract sum analysis is annexed), the articles of agreement, these conditions and the appendices in accordance with the aforementioned documents."

195. In the amended conditions there purported to be a definition of "section". It read: "Section One of the sections into which the works have been divided for phased completion as identified in the Employers' Requirements and/or contractor's proposals."

196. Clause 210 of the Employers' Requirements was entitled "Completion in Sections or Parts". It was divided into three bullet points:

- "where the employer is to take possession of any section or part of the works, and such section or part will after its completion depend for its adequate functioning on work located elsewhere on the site, complete such other works in time to permit such possession to take place;
- during the execution of the remainder of the works, ensure that the completed sections or parts of the works have continuous and adequate provision of services, fire precautions, means of escape and safe access;
- a section of the works will not be accepted for practical completion unless the appropriate number of parking spaces, garages, bin stores, footpaths and safe pedestrian and vehicular access for potential purchasers and owners have also been completed."

197. HH Judge David Wilcox affirmed the Arbitrator's analysis in that clause 17.1.4, which governs the computation of the relief from LADs on account of partial possession, was operable only if a valuation could be placed on the sectional works. The Contract, however, failed to provide any means of ascertaining what was contained in any Section and there was no certainty as to what works comprised each Contract Section. He therefore concluded that it was not possible to value any sectional works and therefore the proportional relief against LADs contemplated was incapable of being calculated. Developers should take heed, and if they require the works to be completed in Sections, they must ensure that it is possible to determine what works are in which Section, including roads and common areas.

Sectional completion and time at large

198. So we see it is not that uncommon for the parties to make a complete horlicks of their sections so that one does not even know what work is in a section, and occasionally there may be doubt over the sectional values and LADs such as to give rise to inoperable LAD machinery and time at large. However, the courts usually strive to make contracts work.

199. In *Liberty Mercian Limited v Dean & Dyball Construction Limited*[60] the issue was the effectiveness of sectional completion schedules that provided for the sequential construction of work sections.

200. A rather loosely worded contract provided for five sectional completion phases. It also provided for liquidated damages at a rate of £12,000 a week for delay. Liberty had hired Dean & Dyball to build four retail units in Aberystwyth. The contractor got into delay but challenged the deduction of liquidated damages.

60. [2009] CILL 2648

201. The claimant Liberty sought declarations as to the proper interpretation of a JCT 98 building contract into which it had entered with the defendant Dyball. Attached to the building contract was a document providing for sectional completion. The work was divided into five sections, each of which was given a date of completion. Section 1 was delayed by a period of eight weeks, so Dyball sought an extension of time. Liberty granted an extension of four weeks and indicated that there was, therefore, a four-week period of culpable delay attributable to Dyball. Liquidated damages were deducted in consequence. A dispute then arose as a result of the consequences of the delay to sections 2 to 5. An extension of four weeks was granted in relation to each of those sections on the basis that Dyball was entitled to an extension of time commensurate with the period of delay for which it was not responsible.

202. However, the four-week culpable delay on section 1 was not the subject of any extension of time on sections 2 to 5. Dyball maintained that it was entitled to an extension of time of eight weeks in respect of those sections, regardless of the circumstances in which that delay arose under section 1. Dyball wrote to Liberty seeking to refer to adjudication the issues on the contract. Dyball maintained that (i) the liquidated damages constituted a penalty because Dyball was repeatedly penalised for the same delay by the deduction of liquidated damages in respect of each section; (ii) the sectional completion schedule was to be disregarded because it failed to identify the date "for" completion in respect of each section and instead referred to the date "of" completion, which was not a term defined in the contract; (iii) since the date of possession for each of sections 2 to 5 was dependent upon practical completion of a preceding section, Dyball was entitled to a full extension of time.

203. HELD: (1) It was plain from the agreement, and from the contractual arrangements as a whole, that both sides would have been aware that the culpable delay of four weeks on section 1 would automatically mean that work on sections 2 to 5 would start four weeks late. The contract did not say in express terms that a culpable delay under section 1 would give rise to a culpable delay, and therefore the deduction of liquidated damages, on sections 2 to 5.

204. However, when considering the contract as a whole, that was what the parties intended to achieve. That was the only sensible interpretation of the sectional completion arrangement, and the only interpretation which gave effect to the parties' clear intention. Such a result could not be regarded as unfair. On the contrary, if a contractor was in culpable delay for four weeks in relation to section 1, which inevitably meant that section 2 was also going to be four weeks late, then the contractor's default had caused the delay to section 2, and he was therefore liable for the liquidated damages that would flow in the consequences.

205. Accordingly, (1) the *liquidated damages did not amount to a penalty*. (2) *The contract had to be interpreted in a common-sense and purposive way. The ordinary reader would not have any difficulty in concluding that the dates of completion in the sectional completion agreement were precisely the same as the dates for completion referred to in the contract*. Accordingly, the wording did not give rise to any difficulty in the operation of the sectional completion arrangement. (3) Dyball sought a full extension of time for the deferred possession, but since the latter only arose in respect of sections 2 to 5 because of the four-week culpable delay, it would be a nonsense to reward Dyball for that delay by granting a full extension of time on the subsequent sections.

206. Declaration granted.

So what are the key points to remember?

207. Sectional completion provisions in contracts should be drafted carefully. Both clients and contractors need to have a clear understanding of the specific risks and obligations that arise as a result of any agreement to complete works in sections. In this regard, robust contract management throughout the entire process is essential.

208. The losses related to each section must take account only of the losses that are related to the delay in obtaining that particular section. There must be an implicit acknowledgement in the LAD clause that losses vary depending on the section of the work concerned.

209. Again, a failure to provide accurate figures of estimated loss tailored to a specific part of the project that is delayed may result in the complete failure of the LAD clause. The courts will be strict when dealing with such clauses and will construe the wording of the clause against the draftsman or the party relying on them. It is also clear that where sectional completion has occurred in practice then the LAD clause will be unenforceable unless it has catered for it specifically.

210. It is not open to the claiming party to cherry-pick so it only wishes to claim a part of the LAD as a way of getting around the fact that sectional completion had occurred but had not been anticipated by the draftsman when the LAD clause was created. In this case the whole clause would fail.

211. Where it is, at the end of the day, impossible to assess a LAD figure then more than likely the court will accept that the LAD sum in the contract is appropriate and enforceable. The rationale behind that rule must be that if the court cannot decide what loss is appropriate then how can it decide that the figure in the LAD clause is inappropriate.

Top Tips

(1) The LAD sums must be a pre-estimate of loss. Try to document the method used for its calculation in case it has to be shown to the court or indeed anyone else when it is used. Try, where possible, to show the calculations to the other contracting party in order that agreement can be reached that it is reasonable.

(2) In contracts with sectional completion dates, LAD figures should be considered carefully and take account of each section's estimated loss.

(3) LADs should never be drafted in such a way where they are a sole or exclusive remedy (*Temloc v Errill*[61]).

61. (1988) 39 B.L.R. 30)

Disputes and 2009

212. Out there in the real world, times are hard. The recession is biting, jobs are being lost and the fit-out, leisure and hospitality industry has been particularly badly hit as private consumers and businesses tighten their belts and cut unnecessary expenditure. However, there are first-class opportunities for those in the industry who have available funds now that their order books are thin to procure construction works. For the first time in years, construction costs are dropping as demand for materials falls as a result of the global downturn. Copper, steel and plasterboard are cheaper now than two years ago. However, with money tight in the system, disputes over entitlement reign and explain the increase in adjudications by most of the ANBs and the frenzy in the Companies Court which each month is seeing many contractors put into liquidation for failing to meet their commitments.

213. I want to look at some highlights with you.

Interpretation of contracts

214. In spite of the apparently well-established rule that when a court comes to construe a contract evidence of pre-contractual negotiations is inadmissible, commentators have suggested that the law in this area is in a state of unrest. The recent House of Lords decision in *Chartbrook Ltd v Persimmon Homes Ltd & Ors*, makes their Lordships' views on the debate clear, and also offers useful guidance on the construction and rectification of contracts.

215. The need to make sure that contracts are completely watertight has been illustrated in this recent case where a dispute over the meaning of a single clause cost a property developer more than £3.5m.

216. In *Chartbrook Limited v Persimmon Homes Limited and Others*[62] the House of Lords was concerned with that chestnut construction of contracts, in particular the exclusionary rule (i.e. that pre-contractual negotiations are inadmissible when considering the proper construction of a contract).

The facts

217. Chartbrook (the Owner) was the owner of a development site, and entered into a development agreement with Persimmon (the Developer) pursuant to which Persimmon was to obtain planning permission in respect of the development site, construct a mixed commercial and residential development, and then sell the properties on long leases. The Developer would then pay the Owner pursuant to a specific formula set out in the development agreement.

218. The Developer accordingly built and sold the commercial/residential development. However, when it came to paying Chartbrook in accordance with the development agreement, the parties disputed the proper interpretation of the formula. The Developer argued that the Owner's interpretation of the formula would result in the Owner receiving a windfall, and that it was entirely improbable that the parties would have made such a bargain (i.e. it made no commercial sense). The Developer also argued that the pre-contractual material (i.e. the various correspondence and documentation between the parties prior to signing the contract) showed that the "windfall" interpretation was clearly not what the parties had commercially intended.

The Court of Appeal decision

219. The Court of Appeal found in favour of the Owner (albeit with one dissenting judgment). The Court's view was that the formula in the development agreement was "clear, certain and unambiguous and its arithmetic is straightforward". The

62. [2009] UKHL 38

Court also found that no exception to the exclusionary rule applied, and thus the pre-contractual material/negotiations were not admissible.

The House of Lords' decision

220. The Developer appealed the Court of Appeal's decision, and the House of Lords unanimously upheld that appeal. They did so on the basis that the Court of Appeal's interpretation of the formula (being in accordance with the Owner's interpretation) made no commercial sense and made the structure and language of the various provisions of the development agreement appear arbitrary and irrational, where it was possible for the concepts employed by the parties in the development agreement to be combined in a rational way. The House of Lords "profoundly disagreed" that the drafting of the formula was "clear, certain and unambiguous" and held instead that the definition was "obviously defective as a piece of drafting". Crucially, Lord Hoffman held that "when the language used in an instrument gives rise to difficulties of construction, the process of interpretation … is to decide what a reasonable person would have understood the parties to have meant by using the language which they did. The fact that the court might have to express that meaning in language quite different from that used by the parties … is no reason for not giving effect to what they appear to have meant." In other words, where it is clear that something has gone wrong with the language in a contract, the proper construction to be applied is that which a reasonable person would have understood the parties to have meant.

221. As such, the House of Lords found for the Developer Persimmon on the construction of the key formula. Usefully, the Law Lords also considered the question of the exclusionary principle. They gave fairly short shrift to the Developer's argument that the current case should qualify as an exception to the exclusionary rule. In various passages of the judgments, their Lordships held that "to allow evidence of pre-contractual negotiations would require the House to depart from a long and consistent line of authority, the binding force of which has frequently been acknowledged" and that the exclusionary rule "could scarcely be more firmly embedded in our law".

Comment

222. The House of Lords' decision was a firm reaffirmation that departure from the exclusionary rule will only be considered in very few, exceptional cases (specifically, where the rule can be considered to be impeding the proper development of the law or contrary to public policy).

223. The emerging trend has been the courts' determination to give effect to the "EC Treaty" principles which underpin the rules of award of contracts by public bodies - in particular, the principles of transparency and equal treatment.

224. The House of Lords confirmed that the rules for contractual interpretation remain:

- what a reasonable person, having all the background knowledge which would have been available to the parties, would have understood them, by using the language in the contract, to mean.
- pre-contract negotiations are inadmissible for the purpose of interpreting a contract.

Cold steel of an injunction

Amec Group Limited v Universal Steels (Scotland) Limited[63]

225. In circumstances where one paying party is for some reason withholding payment from another, it may be attractive for the paying party to refuse to deliver a part of

63. 2009 EWHC 560 (TCC)

its bargain which it recognises to be of value to the payee to create some leverage to encourage payment. The paying party may, however, find itself on the wrong end of an injunction requiring it to perform that which it withheld.

226. As a discretionary equitable remedy an injunction comes only at the discretion of the court to enforce a legal or equitable right. An injunction may take a variety of forms and typically requires someone to stop doing or to do a specified act. An example of a prohibitory injunction would be one requiring a respondent to stop a nuisance like noise passing on to the applicant's property. A mandatory injunction is one that requires the respondent to take steps to reverse the effects of some wrongful act or to take preventative action before it causes the applicant further or any damage.

227. In *Amec Group Limited v Universal Steels (Scotland) Limited* the case concerned an application by Amec for an interim mandatory injunction requiring Universal Steels (USSL) to provide essential QA documentation in respect of four jetty restraint piles and pile caps that it had contracted to fabricate and deliver for installation at a new berthing facility at the Naval Dockyard in Clyde.

228. Due to trouble with USSL's manufacturing subcontractor in China between August 2007 and August 2008, the delivery of the piles had been set back and there were further problems come across in finding an appropriate shipping company. A dispute arose over whether a binding agreement was reached at a meeting on 29 August 2008 resolving the question of payments and an alleged waiver by Amec of its claim for damages against USSL. As a result of a subsequent dispute over payment, USSL elected to retain the QA documentation it was required to provide in accordance with its contract.

229. The case identified a number of major risks in offshore engineering. These included:

- The quality of steel to be used in a marine environment
- The availability of suitable installation vessels
- The availability of working "windows" for marine work.

230. The significance of the QA documentation to Amec was that the MoD needed sight of it before 1 April 2009 to enable installation to progress in May 2009, failing which tidal conditions were such that the next window of opportunity for installation did not arise until October 2009.

231. The application for the injunction was made in anticipation of final determination of the substantive dispute between the parties at a full hearing before the court. The judge noted that this was an application for an interim injunction, in respect of which the leading HL decision in the case of *American Cyanamid Co v Ethicon Limited* [1975] A.C. 396, gave rise to a three-stage test that must be applied by the court. The court must consider:

1. Is there a serious question to be tried?
2. If there is, then the court must go on to decide whether damages are an adequate remedy for a party injured by the court's grant of, or its failure to grant, an injunction.
3. If damages are not an adequate remedy, it is necessary to consider the balance of convenience.
4. Guidance as to the further test applicable to the granting of a mandatory injunction is provided by the case of *Nottingham Building Society v Eurodynamics*

Systems Plc [1993] FSR 468 as follows:

- The overriding consideration is which course is likely to involve the least risk of injustice if it turns out to be "wrong".
- The court must keep in mind that an order which requires a party to take some positive step at an interlocutory stage may well carry a greater risk of injustice if it turns out to have been wrongly made than an order which merely prohibits action, thereby preserving the status quo.
- It is legitimate to consider whether the court does feel a high degree of assurance that the plaintiff will be able to establish its right at a trial.

232. In the present case the judge decided that the injunction should be granted. He reasoned that the dispute over the alleged agreement in August was clearly a serious question to be tried, that Amec did have a high chance of showing that no such agreement was made and that damages would not be an adequate remedy in the event of the court's failure to grant the injunction because USSL was a small company and would be wholly unable to meet the full cost of damages that would likely be incurred by Amec in the event of a delay in installation of the piles from May to October 2009. The balance of convenience lay in granting the injunction so that the installation could proceed. Quick, sensible, and satisfactory. Bang to rights!

Online misrepresentation

Patchett & Anr v Swimming Pool & Allied Trades Association Ltd[64]

233. This next case is a warning to all those who market their construction business on the internet and make statements on their websites as to what the consumer can and cannot expect from the company. It was all about a disclaimer on the website of a pool installers' trade body. The Court of Appeal had to decide whether the disclaimer provided on SPATA's website was effectively brought to the Patchetts' attention to enable SPATA to escape liability.

234. The case was quite complex and entailed a review of the venerable English case law surrounding exclusion clauses, including the case of *Hedley Byrne v Heller*. This old case set out a test for deciding the scope of a duty of care between adviser and advisee. Even though SPATA won, the message from this case is that exemption clauses should be located on the same page as any "advice" given on a website.

The facts

235. In the summer of 2006, Mr and Mrs Patchett were looking to build a swimming pool in the garden of their home. Using Google, Mr Patchett came across the website of the Swimming Pool & Allied Trades Association ("SPATA") in his search to engage an appropriate contractor. SPATA is a well-established, incorporated trade association and its members include most of the major swimming pool installers in the UK. From the website, Mr Patchett obtained the names and contact details of three of its members. Of the three, a quotation from Crown Pools was obtained and accepted and the works duly commenced. Prior to completion, Crown Pools became insolvent and ceased trading, leaving the works unfinished.

236. The dispute between the parties arises out of statements made on SPATA's website. Amongst other assertions, the website represented that Crown was a member of SPATA, that SPATA members have high standards, that Crown had been checked for creditworthiness and the quality of its work and that Crown was a member of SPATA's unique bond and warranty scheme. Furthermore, it stated that this scheme offered "customers peace of mind that their installation will be completed fully to SPATA Standards - come what may!"

64 *[2009] EWCA Civ 717*

237. The Patchetts claimed that they relied upon the representations on the website by choosing Crown Pools and entering into the contract. As it happened, the representations were untrue. Crown Pools was only an affiliate member of SPATA and as such was not covered by the bond and warranty scheme. The Patchetts claimed damages of approximately £44,000 as a result of SPATA's breach of duty to take reasonable care in making these representations.

238. In court, His Honour Judge Worster held that SPATA did not owe the Patchetts a duty of care in making certain statements on its website. The essential reason given was that while SPATA no doubt knew that the representations on their website would likely be acted upon, it would not expect consumers to do so without further enquiry. The website had clearly stated that an information pack, including a contract check list setting out questions for potential tenderers and installers, was available in addition to the information provided on the website.

239. The Birmingham County Court found that the third criteria necessary for establishing a relationship between the maker of a statement and the recipient who relies on that statement, as set out in the case of *Hedley Byrne v Heller*, was not satisfied: "It is known, either actually or inferentially, that the advice [or representation] is likely to be acted upon by the advisee without independent inquiry."

240. The Patchetts appealed against this decision.

The issues

241. Was there sufficient proximity between the Patchetts and SPATA and would it be fair, just and reasonable to impose a duty of care upon SPATA with respect to the accuracy of the statements made on its website?

The decision

242. The Court of Appeal agreed with the conclusions of the Birmingham County Court and dismissed the appeal by a majority of 2:1, with Lady Justice Smith dissenting. The Master of the Rolls, Lord Clarke of Stone-cum-Ebony MR, held that it would be expected that a potential customer would obtain the information pack prior to appointing an installer. He stated that the parties were not in a relationship of adviser and advisee, and as such, there was not sufficient proximity between the parties to give rise to a duty of care. It could not be fair for SPATA to assume a legal responsibility for the accuracy of the statements on the website without the consumer enquiring further, which the website itself encouraged.

243. Furthermore, Lord Clarke held that SPATA had not given a warranty that Crown Pools was at all times creditworthy, but rather that its financial record and previous work had been checked in the past and had been up to SPATA standards.

244. Though academic, it is interesting to note that Lady Justice Smith found that the website did little more than offer the information which was contained in the information pack. She did not see that the website held itself to be merely "the first step in the process" for the consumer to obtain all of the requisite information and respectfully disagreed with the other members of the court.

Commentary

245. This case is an important reminder to those who promote their business on the internet. As the Master of the Rolls reminds us: "It is important that information put into the public domain is accurate." Though it was not the case here, depending on the situation, a company could be liable for false statements and misrepresentations made on its website. Equally, consumers must take care to check all information obtained from the internet. Websites need to be read as a whole and where the

website encourages the obtaining of further information, consumers should certainly do so.

Case details:

(1) *Gary Patchett (2) Karen Patchett v Swimming Pool & Allied Trades Association* [2009] EWCA Civ 717, 15 June 2009, Lord Clarke of Stone-Cum-Ebony MR, Lord Justice Scott Baker and Lady Justice Smith

Fraudulent misrepresentation - failing to inform a client that a team member had quit Fitzroy Robinson v Mentmore Towers

The facts

246. The claimant was an architect seeking payments of unpaid fees in respect of a contract to develop a private members' club and hotel. Contracts had almost been agreed between the parties and so design commenced. The contracts were then signed a few months later, around May 2006. However, before those contracts were signed the team leader had resigned from the architect. The architect eventually informed the developer of the team leader's resignation in November 2006. The developer was not at all pleased, but nonetheless planning applications for the club and hotel were made. Eventually the project was suspended in an incomplete state, and the developer owed fees to the architect for which it served no notice of withholding.

247. Mr Justice Coulson decided that the courts will not allow justice not to be done if the court (the final dispute resolver) is concerned that the sum due is not, in fact, the sum to which the claimant is properly entitled. Mr Justice Coulson thought it would be wrong "in all the circumstances" for him to conclude that the "simple absence" of a withholding notice entitled the claimant to be paid the sum which was technically "due" under the contract, if in fact the defendant had a valid defence as to why this sum should not be paid in full.

248. Given that Mr Justice Coulson thought the defendant had a substantive defence to the full amount claimed, Mr Justice Coulson thought that it would be artificial for him to give judgment for the sum which was "due" under the contract. However, as the defendant was in breach of the contract in failing to pay the sum which was due at the relevant time, the claimant was entitled to be paid interest on those sums which were, contractually speaking, due. The court would determine what amount was "due" at a separate quantum hearing. (The judgment does not say whether interest will be payable at a contract rate, or at 8% over base rate, under the Late Payment of Commercial Debts (Interest) Act 1998.)

249. So, there you go. Section 111 of the Construction Act 1996 does not do exactly everything it says on the tin. No wonder lawyers can never give you a straight "yes" or "no" answer!

The issue

250. The contract provided for payment. Did those instalments need to be adjusted in order to take into account the services that were not completed?

251. In addition, was the architect guilty of misrepresentation in failing to inform the developer of the team leader's resignation. If so, did the developer have a counterclaim for delay, disruption and duplication of work?

252. Finally, had the architect been professionally negligent in relation to the planning application for the club because of the amount of time taken and issues relating to the coordination of the work of others?

The decision

253. The architect's entitlement to fees depended upon the performance of its services. Instalments could therefore be adjusted if the services were altered (in other words, additional services were carried out) or the services were not properly formed.

254. In relation to misrepresentation, the architect's continuing representation of the team leader's involvement became false in March 2006. The architect was concerned that the developer would look elsewhere because of the importance of that team leader. As a result the architect's chief executive officer had made the misrepresentation knowingly and deliberately without an honest belief in its truth. It was therefore a fraudulent misrepresentation. It was material in that it induced the developer to enter into the contracts. The developer therefore had a counterclaim; however on the evidence the only potential loss resulted in the reduction to the fees that were otherwise due to the architect.

255. Finally, the architect had not been professionally negligent. The architect had to coordinate the work of others and had to reasonably see that those others did the work. However, in this instance the architect had not fallen below the standard that one might expect of a reasonably competent architect performing a similar role.

256. The case is interesting what it said about ADR and its willingness to punish, by way of an order as to costs with regard to any party who does not agree to mediate or fails to comply with what is required. Mr Justice Coulson criticised the parties for not having sought to mediate even though there were such substantial differences between them, as they could at least have succeeded in narrowing the issues between them.

Comment

257. The really interesting aspect about this case relates to fraudulent misrepresentation. It is rare to see cases where a judge finds that a party has fraudulently misrepresented the position to a party in order to induce that party to enter into contracts. Here, the importance of the team leader was such that the architect's chief executive officer was concerned the developer would not sign the contracts if they knew the team leader had resigned. The chief executive officer knowingly misrepresented the truth to the developer and so the developer signed the contracts. The chief executive officer was therefore liable for fraudulent misrepresentation leading to a financial claim. In this case, that claim wasn't as high as it could have been, but it serves to remind everybody to ensure they do not mislead the other party when negotiating a contract. Remember also that silence can also amount to misrepresentation where circumstances change. This decision is a warning to consultants and contractors to give careful consideration to the resources that they agree to utilise when carrying out work for a client.

258. Aside from possible claims for fraudulent or negligent misrepresentation, advisers need to consider any conduct rules imposed by their professional bodies and also the potential impact upon their professional reputations.

Case details:

Fitzroy Robinson v Mentmore Towers and Ors

[2009] EWHC 1552 (TCC) QBD Coulson J

Penal rates of interest or not

The facts

259. In this case Master Golf Co ("Masters") bought golf clubs from two ranges through their Far Eastern purchasing agents, Taiwan Scott Company ("Taiwan Scott") for resale in the United Kingdom. Clause 2 of the agreement between them provided for a contractual rate of interest of 15% per year.

260. A dispute arose between the parties as to what sums were due to Taiwan Scott under the agreement.

261. Masters bought golf clubs from Taiwan Scott, who in turn sourced them from the Far East. Masters refused to pay some invoices because it said customers were complaining about the quality. Masters agreed to pay in instalments, but then defaulted. The High Court ordered Masters to pay the balance but refused to award the contractual interest rate of 15% on the basis of it being "an unreasonably high rate, and more inclined towards a penalty then a genuine estimate of loss". Both parties appealed. The Court of Appeal ruled in Taiwan Scott's favour. Interest rates in 2001 were considerably higher than currently and 15% was not exorbitant then. The Court of Appeal added that the High Court was wrong to deny Taiwan Scott a contractual rate of interest which had been agreed between two commercial parties.

The issue

262. Was the agreement for a contractual interest rate of 15% enforceable or was it a penalty and therefore unenforceable?

The decision

263. The appeal as to the disputed payments was dismissed but the cross-appeal in relation to contractual interest was upheld. Longmore LJ emphasised that the interest rate of 15% was either a penalty or it was not. An interest rate cannot be "more inclined towards a penalty than a genuine estimate of loss" as stated by the judge at first instance.

264. Longmore LJ also examined the circumstances at the time the agreement was entered into, commenting that it did not "seem to me that a contractual rate of 15% was in any way exorbitant in July 2001" as, at that time, interest rates were significantly higher. He went on to emphasise that the rate of 15% had been agreed between two commercial concerns in the economic circumstances of the time and should not be set aside lightly. Accordingly, the Court of Appeal held that the contractual interest rate of 15% was not a penalty and interest at 15% was awarded on the amounts held due by the judge at first instance from the date they became due until the date of judgment.

Comment

265. This case is a reminder that it is necessary to assess whether a particular sum or contractual provision is a penalty by reference to the time the contract was entered into and not the date of the breach giving rise to the obligation to pay.

266. At present the statutory rate of interest under the Late Payment of Commercial Debts (Interest) Act 1998 (the "Act") is 8.5% (i.e. 8% over the current Bank of England base rate of 0.5%). Arguably this case suggests that parties to construction contracts being entered into now may be able to agree higher rates of interest than those provided for in the Act if this can be justified in the circumstances. However, a word of caution should be sounded in that this decision was reached in light of

the economic circumstances in July 2001 when, as emphasised by Longmore LJ, interest rates were much higher.

Case details:

Taiwan Scott Co v Masters Golf Company

[2009] EWCA CIV 685 (CA, Civil Division), Longmore, Pill & Richards LJJ

Close - pinch points for JCT contracts in a recession

267. It is clear that the chilly economic climate will last until well into 2010. Where there is an increased likelihood of contractors or employers going "belly up", the provisions of the contract detailing what happens in such circumstances gain heightened significance. This creates significant risks for parties to construction contracts, as some of us saw all too well in the last recession, with the obvious weaknesses of contractors and employers to cash-flow difficulties and insolvency and falling order books and CVRs.[65] These risks increase the importance of the contract provisions in the five areas outlined below, look at them and review them every time you bid and keep them up on the radar. They are worth being on top of every time you step on the merry-go-round, and we will look at some of them in the session:

- Where cash-flow becomes an issue in the course of a project – for example where a contractor needs to purchase materials to complete the job before he has received payment for that job – the provisions in the contract regarding the circumstances in which advance payments, escrows, pre-purchase deeds can also become highly relevant;
- Where the project runs into difficulties, and is stopped part-completed, the question of ownership of the materials used becomes important, as they may be of considerable value to one or all parties; ditto step-in rights of funders and the advent of a "new" client in the shape of a bank with distressed assets;
- The provisions on suspension are dusted off and inspected to see if they are sufficient stick to call a tardy paying employer into line. Often they are not worth the candle of pulling off for the heavier engineering packages and this can be where the biggest holes are burnt in pockets;
- The provisions on termination/determination in the contract detailing how, in what circumstances, and how quickly a party can end the contract or its employment in the face of default by the other party;
- If a contractor is struggling to balance the books, it is inevitable that they will fight hard over any disputed sums in a contract. This can lead to protracted and increasingly bitter litigation. The provisions of the contract relating to dispute resolution will therefore be highly relevant to the success with which the parties are able to remedy the dispute without incurring high litigation costs.

268. One thing is sure; these areas of JCT contracts will be fertile in the trough we have descended into in large parts of the industry. The next decade will be very different from the last for sure!

Simon Tolson
January 2010

65. For those who do not know, CVR is the traditional practice of determining and reporting profitability of a construction project on a regular basis. By comparing costs with value (revenue) at a certain date, you can see the difference between the cumulative profit or loss on the project.