



FenwickElliott

Solicitors

Summer Review 2003

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1. INTRODUCTION – Simon Tolson

Our Summer Review now in its seventh year continues to be very popular. Much has taken place since it started. We have doubled in size and taken new premises. When it began we talked in terms of the future that adjudication would bring to the dispute process. It has now been part of the landscape for over 5 years and we have played a significant part in its history and development to date.

This year's Review inevitably features the continuing impact of adjudication and its steady march to rather more sophistication, formality and legal rigour. A few cases stick in my mind. There was Judge Thornton in *Bovis Lend Lease v Triangle Development* who produced the TCC's puzzle for Christmas when he seemed to have found a daring means of escaping the HGCRA. He held that where contractual terms had the effect of allowing a party to avoid or deduct from a payment directed by an adjudicator, those terms prevailed. However, the Court of Appeal in *Ferson v Levolux* moved swiftly to crush thoughts of escape and took a robust line even where a contract provision as in *Ferson* said all sums ceased to be due on determination of the contractor's employment – enforcement of the adjudicator's decision was allowed.

Much, too, has caught the judiciary's eye, emphasizing the importance of ADR in reducing litigation and the likelihood of trial. There is no doubt a real cost risk if only lip-service is paid to the ADR process; the courts have gone so far as to disallow a winner his costs.

The legal year has been eventful too in the courts, showing their greater flexibility and pragmatic approach to questions of causation and proof of loss than in the past. This trend should assist claimants, in that they will no longer "always" have to prove the causes of their loss as precisely

as they used to. It should also work in defendants' favour, too, as they will be able to narrow the extent of the loss for which traditionally they would have been liable. This trend will be welcome in an industry that has in recent years been trying to simplify claims recovery and reduce the cost and risk of claims. The most significant of these cases is *Fairchild v Glenhaven Funeral Services*, a case concerned with the ghastly but widespread mesothelioma caused by inhaling asbestos mineral fibres, usually in an industrial setting.

The House of Lords allowed Mr Fairchild to recover from one of the two former employers, chosen as the sole defendant since it was the only one that was still in business and trading. Lord Bingham ruled that, in an appropriate case, it is sufficient for a claimant to prove causation and loss against one or both of two possible defendants merely by showing that it is "just and in accordance with common sense to treat the conduct of X and Y in exposing Z [to] a condition against which it was the duty of X and Y to protect him". This ability to recover only arose where both were in breach of a duty owed to Z, the disease was life-threatening and not capable of being caused by any alternative and non-actionable cause, and where medical science could not provide any more accurate means of identifying the cause of the disease.

The case is a watershed and shows, on appropriate occasions dictated by fairness and justice, that the usual traditional basis of recovery involving proof of actual damage could be replaced by one based on an increase in the risk of damage. It does not take rocket science to contemplate the number of construction cases involving joint contract breakers and concurrent causes of loss or delay to which this might be relevant.

We also had some interesting off-the-ball enquiries, two of which I will briefly share with you. One was whether a claim against a valuation surveyor could be maintained because of failure to spot harm caused by mortar bees that had eaten away half the mortar in the gable end of a farmhouse wall. Another came from a publican chain that was concerned about toxic mould (*Stachybotrys Chartarum*) in the converted cellar of one of their public houses. We now know from our American ICLA associate, Peckar & Abramson, that in the States the problem is now so serious it is regarded as “the asbestos of the 21st century”, so watch this space.

You may be excused for thinking domestic arbitration is a quiet backwater these days. Even though most standard form contracts contain an arbitration clause for the resolution of disputes since the HGCRA 1996 came into force, the first avenue pursued by a claimant has tended to be adjudication, not arbitration.

However, given adjudications are running for longer, often 6–8 weeks or more, and emulating arbitration in all but name, it is interesting that there may soon be a new kid on the arbitration block. It is the so-called “100-day Procedure” and will come about by way of a new clause 8A in the CIMAR. Where the parties agree to adopt this new procedure, the arbitrator will have an overriding duty to make his Award within 100 days of the date on which the statement of case is delivered to him or to the other party (whichever is later).

So if you lose an adjudication there is now a real spectre of “going round a second time” but before an arbitrator, and possibly getting the “result” you deserved in the adjudication that did not go to form. We look forward to reporting further on this development in next year’s review.

2. PFI/PPP

Fenwick Elliott Projects Limited

We established Fenwick Elliott Projects Ltd in February 2003 with the intention of providing dedicated legal services in the PFI and PPP sectors. As a firm, Fenwick Elliott has considerable experience of project-related work in this sector and this expertise is made available through the vehicle of Fenwick Elliott Projects Ltd.

Fenwick Elliott Projects Ltd has entered into alliance with other like-minded firms from whom resources, skills and logistical support may be drawn as appropriate, in order to provide clients with an integrated range of services on a nationwide basis.

Our alliance firms presently comprise: freethcartwright (Nottingham and the Midlands); Laytons (Bristol and the South-West); Moorcrofts (Marlow); turnerparkinson (Manchester); and The Project Partnership (London). The geographical spread of these firms means that we are confident that we can offer prospective clients an immediate and tailor-made service at competitive rates.

The Chairman of Fenwick Elliott Projects Ltd is Geoff Haley who joined Fenwick Elliott as a consultant in November 2002. Geoff has wide experience of work in the PFI and PPP sectors: he has been involved in private sector project finance since the mid-1980s and has participated in some of the most high profile, privately funded infrastructure projects. In addition, Geoff is Chairman of the International Project Finance Association, and is therefore well placed to lead the Fenwick Elliott Projects Ltd Team.

Any enquiries concerning Fenwick Elliott Projects Ltd should be addressed to Geoff Haley, Dr Julian Critchlow or Ted Lowery whose contact details appear at the back of this Summer Review.

PPP Forum

On 21 January 2003, Fenwick Elliott Projects co-hosted a very successful Forum with *Building* magazine to discuss current issues facing PPP and explore solutions. Participants included some of the biggest names in the industry, from project developers to bankers and contractors, operators, insurers, consultants and other lawyers.

We set out below details of some of the topics discussed.

The need for PPP

The results of successive government policies over the years have left us with:

- an inadequate road and rail structure;
- health service in constant crisis;
- school and college buildings poorly maintained and rarely replaced; and
- minimum investment in light rail systems for cities.

The Association for Public Service Excellence identified the major problem facing the infrastructure of the UK in its evidence to the Scottish Parliament. It said: “the public sector has been starved of capital investment over a period of 30 years” – in effect, restricted by HM Treasury limits on public debt.

The effect on education in Scotland is all too clear. The Scottish Further Education Council needs £220 million over 10 years to bring colleges up to current health and safety standards. It will take a further £400 million to modernise the estate. Apart from providing insufficient capital, independent studies have now confirmed that the Government’s traditional procurement process was poor.

The Mott MacDonald Report for HM Treasury (published July 2002) identified that government departments had

underestimated project costs and duration or overestimated project benefits consistently on 50 large projects constructed over the last 20 years. In essence, they failed to manage all project risks – most critically, failing to make a credible public sector business case.

Risks arose from inadequate definitions of the projects and the method for their implementation. Insufficient attention to risk analysis and mitigation at the start and failure to consider changes during the project life also contributed to the problems.

In addition, the National Audit Office report issued in February 2003 states that most PFI building work carried out for hospitals, prisons and government accommodation is being delivered on time and on budget. PFI has cut the number of public projects exceeding budget from 73 per cent to 22 per cent.

Where are we now?

The Government faces a public sector borrowing deficit which is likely to be with us for many years.

Public capital for infrastructure investment can only be raised through yet higher taxes – hardly palatable to the electorate when other more acceptable options exist.

Irrespective of union opposition to the transfer of public sector members to the private sector, the Government has made it clear that the PPP process is being used to hasten public sector reform.

The Government’s commitment to provide new hospitals and schools relies heavily on the PPP procurement route.

The largest ever hospital building programme is now under way. The National Health Service’s Ten-Year

Strategy Plan published in July 2000 promises the construction of 100 new hospitals before 2010, as well as 20 diagnostic and treatment centres, 500 one-stop primary care centres and the refurbishment and replacement of up to 3,000 family doctors' surgeries. Some £7 billion of new capital investment is required through the PPP procurement route by 2010.

In education, it is a similar tale. The Government expects PPP to improve the run-down school estate by providing new investment, better quality buildings and services, innovation to widen usage and benefit the community, and greater efficiency.

In England, PPP commitments to 2005–6 involve the building or refurbishment of over 500 schools at a cost of £2.4 billion. Most centrally funded new schools involve PPP.

Key benefits of PPP

For the Government

- Keeps debt down.
- Frees up capital to spend on other government services.
- Retains strategic control of the overall project and services in the public sector.
- Assists in the reform of the public sector.
- Assures that fixed price construction contracts are completed on time and at cost with minimum variations.
- Transfers the risk of performance of the asset to the private sector. The private sector only realises its investment if the asset performs according to its contractual obligations.
- Focuses the procurement process on the whole life cost of the project and not simply on its initial construction cost. It identifies the long-term costs

and assesses the sustainability of the project.

- Defers payment over the contract life (usually 25 years).
- Enables investment decisions to be based on fuller information as it requires a detailed analysis of project risks by both the Government and lenders at the outset. Cost estimates are robust.

For the public

- Gets access to improved services in health, transport and education now, not years away when the Government's spending programme permits.
- Avoids paying higher taxes to finance infrastructure investment.
- Enjoys a higher standard of finish. As the private sector operates the project for the concession period, more attention in the design is paid to maintenance and repair aspects.

Issues

Between them, the Forum and the IPFA survey identified a number of key issues which need to be addressed to make the PPP process more efficient and effective in the future. These focus on bidding, insurance, design, documentation, public sector decision making and procurement training.

Bidding

Confidence: Some 88 per cent of respondents to the IPFA survey on the future direction of UK PFI believe that the number of contractors bidding for future PFI schemes will decrease. That will be of little comfort to a Government whose policy in health and education is wholly reliant on private capital investment through the PPP route.

Forum participants felt that the banking sector was currently nervous of PFI – unsettled by the fact that some energy loans were in default, falling share prices and the general economic malaise. However, the withdrawals of Bank of America and Abbey National from the PPP market were accepted as strategic moves by those companies with little, if any, detrimental effect on the PPP market. The participants also recognised that banks move in and out of the market for other reasons. However, adverse press coverage of projects contributed to City nervousness and lack of confidence.

On the optimistic side, there are a great many deals around and new financing products are being developed in the capital markets.

Costs: New accounting rules and the well publicised problems of contractor, Amey, prompted participants to discuss the question of bid costs. The bid costs for the London Underground have now reached £300 million of which the Tubelines Consortium has spent some £140 million. Some project promoters and contractors accepted the principle that high bid costs for entering the PPP market reduce competition. On this basis, successful contractors do not want to see bid costs reimbursed by the Government, while unsuccessful contractors do.

However, the general consensus was that high costs exclude parties that do not have the means to enter the expensive bidding process. In the long term, this is detrimental to the procurement process. The large number of hospitals and schools needing financing, together with highways, light and heavy rail, could lead to a lack of bidding capacity in the market. Main contractors would be able to “cherry-pick” projects, while small contractors would be left out.

Reducing bid costs

They agreed that the PPP market is changing and reforms are required. Participants were particularly concerned to reduce bid costs and offered a range of potential solutions:

- Reducing stages for tender.
- Reducing time up to best and final offer.
- Eliminating the best and final offer stage.
- Reducing number of bidders to two or three.
- Developing the brief as fully as possible with improved project definition before it is issued to bidders.
- Reducing the need for detailed design up front.
- Moving design to best and final offer stage.
- Encouraging contractors to withdraw from projects if the design becomes too prescriptive.
- Increasing public sector knowledge.
- Standardising contracts, where appropriate.
- Ensuring government departments do not ask bidders and lenders for full due diligence before preferred bidder stage.
- Using a binding bid timetable with incentives for compliance.
- Putting public sector advisers working “at risk” to financial close on par with private sector.
- Fast tracking invitation to negotiate process.

On the other hand, government departments argue that they need as much information as possible during the tender process before selecting a preferred bidder. This places competitive pressure on the parties and ensures that maximum information is released before selection takes place. In the case of the Local Improvement Financial Trust (LIFT)

programme, the health sector accepts that the costs of entry have been high. However, the market has been structured as a new business sector offering a 20- to 25-year business stream with a series of 10 to 20 projects over that period. In return for high bid costs, the private sector will obtain a known market share in a sector. The Department for Education has indicated its concern that bidding capacity may fall in the future. It is looking at similar models to LIFT to improve the provision of its own capital programme.

Innovation in PPP

Forum participants envisaged further improvements and innovation in the PPP market as it matures. They pointed to bond issues being introduced in competition with commercial bank lending and, thereby, revolutionising the financing market. Some innovations – such as funding competitions – were seen as discouraging value for money and competition. However, most saw secondary funds, such as the Abbey National and Babcock & Brown Fund, as innovative and a useful structure to release sponsors' funds to improve market liquidity. They welcomed improved contracts and guidance from government departments.

Some participants commented that PPP is not a panacea for all projects. In the case of the numerous projects with a capital value of under £10 million, it proves to be a complex method of procurement. The market may benefit if other, less complex methods are developed. But the present Government public sector borrowing deficit, likely to be with us for many years, means PPP is here to stay.

Winning support for PPP

The effectiveness of PPP depends on addressing the key issues identified earlier – and in winning over the sceptics in the

media and the great British public. The media have shown a consistently adverse and negative approach to the PPP process. Participants agree that it is very difficult to persuade the media to talk about the benefits of PPPs and the 500+ problem-free schemes under operation or construction. They felt that the successful delivery and performance of new projects will probably be the best way to convince the media – and the public at large – of the enormous benefits of the PPP process to the economy, infrastructure and well-being of this country. They suggested that the industry should advertise the new schools, hospitals and roads with notices on buildings clearly indicating that these are provided under the PPP process. The industry should tackle trade union opposition head-on by illustrating that the private sector delivery, performance and efficiency of these projects has substantial benefits for union members.

3. MEDIATION

As Simon Tolson indicated in his introduction, the courts have repeatedly over the last 12 months re-emphasised the importance of ADR. *Richard Smellie*, in an extract from a paper given at the Second Global Project Superconference in May 2003, gives an insight into what mediation actually is and why it is increasingly moving into the mainstream and forefront of dispute resolution.

Effective Dispute Resolution

The notions of mediation and conciliation have been in operation in legal systems for some considerable time: for example Japan has had a conciliation law since 1951 which allows for court proceedings to be transferred to a process of conciliation, and in the West, have been operating in the United States since at least the 1970s. Tribal courts in Africa operate what might be called a “conciliation philosophy”, being “future

orientated” in that they look at how people will continue to live in harmony beyond their dispute, and so seek to restore the “social balance” through compromise and reconciliation rather than the application of rules of law.

What is new, however, is the fast growing interest and application of alternative dispute resolution techniques, and in particular mediation and conciliation, in international commercial disputes, and the ever-increasing acceptance of these ADR techniques as a “mainstream” means of dispute resolution in the UK and Europe, as well as elsewhere.

This is something of a cultural change in both the domestic market and the international market. The use of mediation, because of its very nature, does require an understanding of approach and a desire to resolve disputes outside of an adversarial and formal procedure, focusing on the best means of appropriate satisfactory compromise for the good of all concerned, rather than strict legal rights.

ADR, and in particular mediation, has an ever-increasing role to play in the resolution of disputes, and indeed in the avoidance of disputes. As a matter of important housekeeping, that which falls under the banner “ADR” does vary depending on whom you are talking to, but most see it as covering any form of dispute resolution other than proceedings in court or “ordinary” negotiations.

What is mediation?

Mediation is essentially structured negotiation. Mediation is therefore a dispute resolution technique in which, with the assistance of an impartial third party, the parties seek to resolve their differences through compromise.

It is a private, uniquely flexible dispute resolution process concerned with finding a solution satisfactory to all involved. Its primary characteristics are:-

- a) It is a consensual process, with the procedure being a matter of agreement between the parties.
- b) It is an entirely private and confidential process, conducted on a “without prejudice” basis.
- c) It is generally a voluntary process, in that after the dispute has arisen, the parties agree to mediate the dispute.

It should be noted, however, that more and more a requirement to mediate is being written into the dispute resolution provisions of contracts; but the process remains voluntary in that the procedure will often allow a party to withdraw from the process, and it remains concerned with compromise and not the imposition of a decision by a third party.

- d) As just said, mediation is non-binding: its objective is to broker a settlement deal, and there is no decision made by a third party which is then imposed on the disputants.
- e) It is the role of the mediator to facilitate compromise. The mediator is an impartial third person. His role is described by the Centre for Effective Dispute Resolution (CEDR), in their *Mediator’s Handbook*, as follows:-

“The Mediator helps the parties to try to reach a negotiated settlement. The Mediator provides a clear head, impartiality, process management, encouragement and optimism, and brings hope to a situation that may seem hopeless, whilst leaving the problem and the settlement decision firmly with the parties.”

The CEDR handbook goes on to refer to the mediator as a facilitator, a reality tester, a problem-solver, a “sponge” for

the parties' frustrations, and a scribe to help accurately record the settlement reached.

In many respects, the techniques used by a skilled mediator have more in common with international political diplomacy rather than mainstream legal culture. The "shuttle diplomacy" of international politicians brokering significant international arrangements is the kind of technique which skilled mediators use in going from caucus session to caucus session in a mediation.

Types of mediation

Mediation might be facilitative or evaluative.

In a facilitative mediation the mediator seeks to facilitate the parties' own efforts to formulate settlement, whilst in an evaluative mediation the mediator further assists by introducing his or her own view on the merits of the case, in some instances providing a written recommendation. It is probably fair to say that facilitative mediation is more common for the resolution of mainstream commercial disputes, save that the "hybrid" of "mini-trial", where the parties present their respective cases to a panel of executives and a neutral, caucus sessions are then held, and the mediator makes recommendation, is not uncommon in commercial disputes.

Procedure

The mediation procedure followed by the parties is dependent upon agreement by the parties. This agreement might or might not be found in the dispute resolution provisions of any contract between the parties.

Mediation strengths

The first great strength of mediation as a technique for the resolution of

commercial disputes is that the parties seek their own solution through a flexible procedure, aimed at encouraging positive compromise rather than the imposition of law. The parties have control of the process and its outcome, and whilst any settlement must be within the law, it does not have to reflect the parties' strict legal rights and can take into account commercial and political pressures and realities. Consequently:-

- a) The parties do not have to seek redress entirely in the form of monetary compensation, and
- b) The parties can seek to rearrange their contractual/commercial arrangements in order to facilitate or bring about satisfactory or indeed a "win-win" solution to the dispute, and
- c) The wider social and/or political implications and/or difficulties can be taken into account and both reflected in and, if possible and appropriate, included within any compromise.

Mediation is in line with the commercial world's recognition of the benefits of partnering, business alliances and general relationship marketing. The flexibility of mediation allows these factors to be taken into account in the resolution of any dispute.

The second great strength of mediation is the cost and time benefit, particularly as against arbitration (be it domestic or international) and litigation in the local courts – and particularly in those jurisdictions where the court process remains not only expensive but slow.

In many instances, from the moment of agreement to mediate through to the conclusion of the mediation, little more than one or two months might pass. This is necessarily dependent upon the nature of the dispute and the extent to which the parties have already put forward their

case. So for example, where arbitration or litigation is already up and running, a mediation might take place within a matter of weeks, whilst where the dispute is still being formulated, there may be a need for the parties to take time to properly ascertain issues before a useful mediation can take place.

The mediation itself, however, will often take no more than two days, regardless of the amount involved. In the introduction to *International Mediation – the Art of Business Diplomacy* (Kluwer Law International, 2001, Carroll and Mackie), the authors say:-

“Most telling in terms of mediation’s future scale of impact, the range of case values is wide – \$200,000 to \$500 million, the average length of mediation just under two days.”

As against the cost and time of litigation or arbitration (be it domestic or international), mediation is profoundly efficient.

Mediation’s third great strength is that it is very much an alive and developing dispute resolution technique as is clear from its move into mainstream dispute resolution.

Mediations move into the “mainstream”

Mediation in the United Kingdom and in Europe has clearly moved firmly into the mainstream of dispute resolution in the past few years.

Firstly, following Lord Woolf’s “Access to Justice”, direct express reference to ADR has found its way into the court rules for England and Wales, being the Civil Procedure Rules 1999 (CPR). Uniquely, these rules commence with an “overriding objective”, being a statement that the rules are a code “. . . with the overriding objective of enabling the court to deal with cases justly”. CPR 1.4 then provides as follows:-

“(1) The court must further the overriding objective by actively managing cases.

(2) Active case management includes . . . (e) encouraging the parties to use an alternative dispute resolution procedure if the court considers that to be appropriate and facilitating the use of such procedure.”

Further, in consequence of the overriding objective in the CPR, pre-action conduct is of considerable importance now in English courts when it comes to the issue of costs. The decisions of *Dunnett v Railtrack Plc* [2002] 1 WLR and *Hurst v Lemming* [2001] EWHC 1051 (CH) both confirm the importance of parties properly and fully considering mediation and, indeed, engaging in mediation unless they have good reason not to, in advance of litigating. Further, they confirm the recognition which mediation now has. The following extract from the judgment of Brook LJ in the *Dunnett* decision perhaps highlights the “new” judicial view of mediation:-

“Skilled mediators are now available to achieve results satisfactory to both parties in many cases which are quite beyond the power of lawyers and courts to achieve. This court has knowledge of cases where intense feelings have arisen, for instance in relation to clinical negligence claims. But where the parties are brought together on neutral soil with a skilled mediator to help them resolve their differences, it may very well be that the mediator is able to achieve a result by which the parties shake hands at the end and feel that they have gone away having settled the dispute on terms with which they are happy to live. A mediator may be able to provide solutions which are beyond the powers of the court to provide.”

The mainstream acceptance of mediation can be further seen in its inclusion in the OGC’s *Dispute Resolution Guidance* from March 2002. This document provided a government pledge that government departments will consider the use of alternative dispute resolution in all

suitable cases, and that government departments will provide appropriate clauses in their standard procurement contracts on the use of ADR techniques to settle disputes. The impetus for this pledge lies in the recognition, as set out in the introduction, that:

“Contractual disputes are time-consuming, expensive and unpleasant. They can destroy client/supplier of relationships painstakingly built up over a period of time and can impact the supply chain. They can add substantially to the cost of the contract as well as nullifying some or all of its benefits or advantages. They can also impact on the achievement of value for money. It is in everyone’s interest to work at avoiding disputes in the first place and this is mirrored in the government’s emphasis on improving relationships between the client and supplier through teamwork and partnering.”

The *Dispute Resolution Guidance* covers ADR (and the scope of ADR as seen by this document is set out above). The inclusion of mediation, however, draws mediation firmly into the mainstream dispute resolution techniques to be used by UK government departments. Indeed, at paragraph 7.1 the guidance says of mediation:-

“It should be seen as the preferred dispute resolution route in most disputes when conventional negotiation has failed or is making slow progress. Mediation is now being used extensively for commercial cases (including cases involving government departments), frequently for multi party and high value disputes. Over 75% of commercial mediations result in a settlement either at the time of the mediation or within a short time thereafter.”

In February 2003, it was clarified by Baroness Scotland of Asthal, the Parliamentary Secretary for the Lord Chancellor’s Department, that following the pledge, alternative dispute resolution by government departments has increased dramatically from 49 cases in 2001–2 to 225 cases. She said that “progress on this

scale clearly demonstrates that the pledge marks a step on the road away from a culture of litigation towards a culture of settlement”.

Turning to the wider picture of Europe, the European Commission’s Green Paper on Alternative Dispute Resolution in Civil Commercial Law from April 2002, quoted from above, has been adopted in draft by the European Parliament.

With further reference to PFI and concession contracts, although the general guide (from the OGC and Partnership UK) on the standardisation of PFI contracts (from August 2002) makes no mention of mediation other than in a footnote, mediation is now expressly included in some proposed PFI standard form dispute resolution provisions. For example, the Centre for Effective Dispute Resolution (CEDR) *Standard Dispute Resolution Procedure for PFI and Long Term Contracts* (September 2002) includes mediation, and it is understood that mediation is to be included in the new JCT Major Projects Form of Contract.

Perhaps the strongest indication as to how “mainstream” mediation has become, and its continuing growing importance, is the announcement by the English Court of Appeal on 10 March that it has appointed CEDR to relaunch its mediation scheme. The relaunch follows limited success, but there is clear determination that there be both a procedure and a “culture” of looking to mediation, in appropriate circumstances, following the decision of a court of first instance.

Finally, whilst mediation is not mandatory in the United Kingdom it is not beyond the realms of sense and possibility that it could be in the future. It is interesting to note the conclusions of an evaluation committee in Canada in March 2001, regarding the inclusion of a rule in the Canadian Civil Rules mandating a

mediation session for case managed actions within 90 days of filing of the first Statement of Defence. The recommendation of the Committee was that, essentially, the rule be included (albeit that as a matter of detail various changes were suggested).

The Mediation Experience

As it is now clear that the courts require you to give consideration to adjudication, *Peter Webster* considers some of the commercial realities of actually agreeing to mediate a dispute. The first of these is of course cost.

This is a fair commercial question and, unsurprisingly, one that we often get asked. In *Malkins Nominees v Societe Finance* a party lost 15 per cent of their overall cost recovery after refusing an offer of mediation – but how does this figure compare to what I have to spend in irrecoverable costs to participate in a mediation?

The costs of mediation can be considerable, as can the time required to prepare for it in order to clarify the issues and the law and evidence relevant to them, just as they can be for any hearing at court. If the commercial risk assessment is made on the basis described in the last paragraph, then the scales may well tilt in favour of refusing mediation.

This assumes, however, that mediation – if attempted – will fail to settle the dispute. Advocates of mediation will draw attention to the 30 per cent of costs that are routinely disallowed to successful litigants at the end of a trial, and of course to the risk of losing at trial and being ordered to pay the other side's costs of the trial, and ask whether commercially one can justify *not* attempting a process which could settle the matter there and then. The leading UK body promoting mediation, the Centre for Effective

Dispute Resolution (CEDR), recorded a settlement rate of 54 per cent in the 41 construction cases for which it provided a mediator during 2001–2 and 65 per cent on the day or very shortly afterwards in 2002–3, figures which are some way below the 77 per cent settlement rate for its caseload as a whole (a discrepancy which it attributes to the increasing complexity of construction cases), but still high enough when combined with the risks of proceeding direct to court to make a serious evaluation of whether mediation would have a reasonable prospect of success commercially sensible.

Commercial clients will also be aware that a party taking a decision which both parties are aware strengthens the other party's negotiating position lessens the chances of a negotiated settlement on favourable terms for the party taking the decision. If mediation is undesirable for one party, that party needs to give thought in the usual way to whether it might be even more undesirable for the other party. Don't be the first to blink – it is better to have no mediation with the other party shouldering the costs risk than to have no mediation with that risk assumed by yourself.

Effective negotiation

Mediation is essentially facilitated negotiation. For this reason, however, parties can assume that because negotiations have got nowhere, mediation will be equally fruitless. This is not always a fair assumption for a number of reasons.

First, parties in direct negotiations tend to focus upon their positions, to the point where it can be very difficult to “climb down” without losing face. Litigation is the logical outcome of this approach, as in court the judge generally upholds one position and rejects the other. In a mediation, however, the mediator can also

encourage the parties to consider the underlying interests behind their positions, and explore options which could satisfy both sets of interests. This can make a crucial difference where one party is in financial difficulties, as is often the case in construction disputes.

If your success in adjudication or court proceedings forces your opponent into liquidation, and you have no security for the sums awarded to you, then you will probably pay a high price for the satisfaction of being found to be right. It can also make it easier for a party defending a claim for professional negligence to make an offer to settle, as it is in their interest to avoid the publicity associated with a trial even if they have an arguable defence.

The mediator, as a neutral third party guaranteeing confidentiality to both sides, can be told about these kinds of interests which would often not be admitted in direct negotiations, and can discuss possible solutions which would cater for them.

Second, a dispute often carries with it collateral damage to the business relationship between the parties to the dispute, which in turn makes constructive communication and commitment more difficult. From the perspective of one if not both of the parties, they have entered into an agreement with the other party, and that other party has failed to perform in accordance with the terms of the agreement.

Why then, they ask themselves, should they trust this reprobate party again, and conclude a further agreement with them in settlement of the dispute? If the other party says they should trust them and do a deal because the alternatives are worse, then that may sound a bit rich even if the logic is inescapable, but if the mediator establishes this in a discussion with that

same party, then it may be a lot easier to move forward on that basis.

Third, as decided by the courts in *Cable & Wireless plc v IBM UK Ltd*, an agreement to mediate is viewed by the courts as enforceable, whereas an agreement to negotiate is not. This can make a significant difference in cases involving large numbers of parties (not uncommon in the construction industry where everyone involved in a project can be sued by the client if something goes wrong).

The reason for this is that it makes possible one concerted effort by all parties to settle the dispute, which might otherwise be impossible when the logistical difficulties of getting decision makers in various companies to consider the matter, and the inclination on all sides towards positional bargaining, are taken into account. These kinds of disputes can simply be viewed as “too complicated” by those with authority to negotiate a settlement to them, but the efforts of a mediator can sometimes resolve them with surprising ease.

Willing agreement

In the context of a construction dispute, adjudication must be considered the principal form of alternative dispute resolution. It is a statutory right, and it guarantees a swift and relatively inexpensive decision within a month of a dispute being referred to an adjudicator. As the decision in *Carter v Nuttall* makes clear, the right prevails over any agreement to use another form of dispute resolution. Assuming that the dispute is under a contract to which the adjudication provisions of the HGCRA 1996 apply, is there any reason to prefer other alternative means of dispute resolution?

One of the most significant features of mediation which is commended by some

of those involved in the process and bemoaned by others is that it gets rid of disputes, rather than resolving them. The downside is given by Tony Bingham in his column in *Building* magazine (9 May 2003) as follows:

“Mediation is known as alternative dispute resolution – that title is misleading. It is an alternative to litigation, arbitration or adjudication because those decide whether someone has broken their contractual promises and they calculate the damages. You can have the alternative to all those by negotiating a deal that ignores broken promises, ignores how disappointed you are, ignores how angry you have become and tells you that you still can’t afford the English legal system.”

The positive side is that although a judge, adjudicator or arbitrator may make a decision on the rights and wrongs of a dispute, he will not necessarily convince the losing party who has invested large amounts of money on solicitors’ and barristers’ fees and has used up large amounts of management time – some of it under fire in cross-examination by the opposing counsel – that his decision is just and founded on truth, and the “resolved” dispute may continue to be a bone of contention between the parties (particularly if it has made a large dent in the losing party’s accounts); whereas after a successful mediation, both parties will have consented freely to the outcome, even if it was not ideally what they would have wanted.

The construction industry is a small world, and parties who are in dispute under one contract may well be engaged in a tender process for another one. In this context, it is clearly unlikely to be helpful to give your potential future employer or contractor a bloody nose just for the sake of proving you are in the right.

There will be situations where the potential margins on future contracts do not justify the compromising of a dispute under an existing one on the terms offered, but even here, mediation offers the opportunity to approach the existing contract in the same way as the potential new one: by a mutual attempt to reach agreement.

On the other hand, the future opportunities may be so lucrative that it would appear to be the height of folly to rock the boat by pursuing a dispute under a comparatively insignificant existing contract, and here mediation can be an efficient, non-confrontational way to get rid of the dispute without simply capitulating.

Conclusion

Put at it simplest, mediation offers the parties to a dispute the chance to get back to where they started their relationship: with an agreement about the matters on which they wanted to do business. The involvement of a third party such as a judge, arbitrator or an adjudicator to make decisions for the parties involves a tacit admission that the parties have lost control over their own contractual relationship. It is often a more effective means to this end than negotiation because “two heads are better than one” for each of the parties seeking a resolution to a dispute. The extra “head” also has the confidence of the opposition, if he or she is doing their job well – just as the other party would have done when entering into the original contract under which the dispute has arisen.

It is often more beneficial to both parties than court proceedings because of the flexibility the mediator has to help the party to tailor a solution to their respective interests, unlike the judge who has to declare a winner and a loser, and sometimes two losers if one party goes

insolvent as a result of his judgment. As the procedural rules of the court and the decisions of the judges indicate, it is not an option that should be passed over lightly in the attempts to resolve a dispute.

Contracted Mediation

In last year's edition of the Summer Review we referred to several important cases concerning mediation. We also reported upon the new development of "contracted mediation".

We have witnessed some developments in the area of contracted mediation during the past year. Contracted mediation, which is sometimes referred to as "project meditation", builds upon the concept of dispute avoidance and early dispute resolution in one simple procedure. Two mediators are appointed at the commencement of the project. One is a lawyer and one is a commercial construction expert. Both of them are trained mediators. At the outset of the project the panel of two mediators conducts a workshop, introducing the employer, contractor and design team, as well as the key sub-contractors, to the concept of contracted mediation. The mediation panel members should therefore be able to develop a working knowledge of the project and also the individuals that are working on that project. If any dispute or difference arises, the panel is immediately on hand to assist the parties to search for a solution to the problem.

Since reporting last year on the collaborative research between Fenwick Elliott and King's College, Nicholas Gould of Fenwick Elliott has been appointed (along with a construction professional) as a mediator to a contracted mediation panel. The major project started last year, with a duration of approximately 2 years. A key individual from one of the parties has stated that he

believes that the mediation panel assisted in avoiding disputes which would otherwise have developed, and also improved team relationships.

While there is of course the cost of employing the mediation panel during the course of the works, this is often negligible compared to the costs of the project, and the potential cost of not just the formal disputes but also the delay that can occur to projects because of clashes in personality which, in turn, affects the performance of the individuals working on the project for its duration. It remains to be seen whether the process of contracted mediation will develop further within the construction industry.

Construction Conciliation Group

The Construction Conciliation Group ("CCG") was launched on 1 May 2003. The CCG's aim is quite simply to provide a cost-effective dispute resolution procedure principally aimed at disputes concerning residential occupiers and their builders (or disputes between residential occupiers and their architects or other professionals).

The adjudication legislation does not cover disputes involving residential occupiers. In the absence of a contract, such as the minor works contract which contractually provides for adjudication, disputes between residential householders and the builders end up in the County Court. These disputes are often (although not always) of low value, such that the legal fees are disproportionate to the amount in dispute. However, legal fees are not the only issue in respect of these types of disputes.

The Chairman of the CCG has noted that *"such disputes are often highly emotionally charged. They have the capacity to absorb considerable time and costs which frequently end up exceeding*

the sums in dispute.” The essentials of the CCG procedure provide:

- A pre-agreed, fixed period with a fixed price process.
- A fixed period of 28 days within which a fixed duration mediation is to be held. If no agreement at the mediation, then a binding enforceable recommendation is made by the conciliator (subject to later litigation/arbitration). The amount of documentation is severely limited.

The parties can simply log on to the website (www.ccggroup.org.uk) in order to choose a conciliator. The rules can be downloaded for free. If the parties cannot agree upon a conciliator then the Group will appoint one for a fee of £50. The fixed timescale and fixed fee is aimed at introducing an economical manner for the resolution of these disputes.

Further, in the absence of a mediated settlement, the parties know that a recommendation will be made based upon the documents, submissions and representations made. If one of the parties does not wish to accept the recommendation then that party must issue a notice of dispute within 28 days of the recommendation and also take steps to commence either legal proceedings or arbitration within three months, otherwise the recommendation will become finally binding.

The CCG hope that the procedure will provide an economic manner within which to resolve construction disputes with homeowners. The procedure can of course be used for any construction dispute should the parties wish to adopt the CCG’s conciliation rules.

For further information contact the publicity officer, **Nicholas Gould**, at Fenwick Elliott.

4. ADJUDICATION

Fenwick Elliott Update Seminars

We continue to hold regular Update Seminars at the Savoy. The next, to be held on 10 November 2003, will be our eighth. Recent guest speakers have included HHJ LLoyd QC, HHJ Kirkham, Geoff Brewer and John Uff QC.

Dr Julian Critchlow, in our sixth Seminar in January, addressed some of the criticisms of the adjudication process in an entertaining and thought-provoking paper, an extract from which is set out below:

It’s Not Fair: What Can I Do?

So, let’s start by asking what fairness is. Well, it seems to me that that is a question that bristles with difficulties. For a start, it depends very much on who’s asking the question. A barrister might say that a fair result is one where his client wins and he makes a lot of money. And given that it’s been said that the difference between a barrister and a solicitor is about as marked as the difference between a crocodile and an alligator, solicitors might well share the same view of fairness.

However, I suspect that many of you would not see fairness in that light. I expect, though you can say at the end if I’m wrong, that a more popular idea of fairness is a procedure that produces a result that accurately reflects the legal and factual merits of the case. That is, it is a way of finding out who’s right. Of course, you might say that just because a decision is legally correct it doesn’t mean that you would necessarily regard it as fair – it’s well known that the law is quite capable of looking an ass. That’s why many jurisdictions (including our own – Arbitration Act 1996 section 46) allow the parties to arbitration to agree equity clauses by which the arbitrator can

sometimes override the strict law by applying his own idea of fairness instead. However, what I want to talk about today is procedural fairness: the things that a tribunal has to do in order to arrive at a correct result, whatever the criteria for a correct result may be.

And the next problem that that throws up is that all procedures inevitably take time and cost money. And if it takes you several years and tens of thousands of pounds to get a decision, the fact that it's the so-called right decision isn't going to stop the whole process looking extremely unfair: in the well-known phrase, justice delayed is justice denied. Now, in recent years, there has been a general move in all areas of dispute resolution towards seeing fairness as not being limited to getting the right result. Instead, it is increasingly seen as a balance of the competing requirements of time, cost, and accuracy of decision. For example, in the English High Court, the CPR states that cases should be dealt with in a way that is proportionate to:

- (i) the amount of money involved;
- (ii) the importance of the case;
- (iii) the complexity of the issues; and
- (iv) the financial position of each party.

Similarly, the Arbitration Act 1996 section 1(a) lays down the fundamental principle that "the object of arbitration is to obtain the fair resolution of disputes by an impartial tribunal without unnecessary delay or expense".

But what about adjudication? How has adjudication developed in the context of procedural fairness? Well, it seems to me that the hand of public policy is plainly to be seen in the way that the courts are sculpting the entitlement of the parties to fairness, and the obligations of the adjudicator to act fairly.

Now, it's well known that the original rationale behind adjudication was to protect contractors' and sub-contractors' cash flows and to ensure that roughly the right amount of money went into the right pocket on a quick and dirty basis.

The core of this idea can be found back in the Latham Report. Central to it is the idea that a fair system needs speed and cost-effectiveness as well as accuracy. It was felt that it did not matter if decisions were approximate because any errors could be put right in subsequent litigation or arbitration.

In furtherance of that aim it seemed, in the early days, that the adjudicator was given by the Housing Grant Construction and Regeneration Act 1996 very wide latitude as to how he could conduct the process. He only had 28 days to reach a decision and so he obviously wouldn't have time to follow the court model of having pleadings, disclosure of documents and the like. He would have to cut corners.

So, in that context, it seemed significant that the HGCR Act said nothing about the adjudicator having to act "fairly". All the Act said was that he had to act impartially (section 108(e)), and that he would be entitled to take the initiative in ascertaining the facts and the law. Now, although the fairness obligation was not expressly stated in the Act, it is likely that some general obligation of fairness going beyond the mere obligation not to be biased was always going to have to be implied into the adjudication process.

By way of analogy, as Lord Loreburn said in the administrative law case of *Board of Education v Rice*, the requirement to act in good faith and listen fairly to both sides is "a duty lying upon anyone who decides anything". And the reason for that minimum requirement of fairness in all proceedings affecting legal rights is, it

seems to me, squarely linked to the imperative that we've already looked at that, namely that the result should reflect the merits of the case so far as is possible given time and cost restraints. So it's not enough for the adjudicator to be unbiased. He must also try to find out who is right and who is wrong. Otherwise, he could impartially toss a coin to decide.

You could end up with the process referred to by Lord Bingham in his 1989 Freshfields Lecture (and brought to my attention by John Uff QC), where he referred to a form of arbitration purportedly flourishing in County Down in the nineteenth century whereby the outcome of a dispute was determined by a turkey choosing a grain of corn positioned closer to one or other party.

Lord Bingham said:

"...this form of arbitration, although perhaps unattractive to professional arbitrators, has in large measure most of the merits claimed for this form of dispute resolution. It is very inexpensive, the more so because the bird can be used again. It is private. It enables the parties to select an expert tribunal. It minimizes the opportunities for judicial intervention. And it promotes the expeditious determination of references."

However, the Lord Loreburn definition of fairness would nevertheless give an adjudicator very wide discretion as to how he conducted a case. In particular, it would not, for example, necessarily prevent him from speaking to one side in the absence of the other. But, in fact, the recent cases on adjudication show that the courts are starting to construe the adjudicator's obligation to act fairly in a rather more technical and restrictive way.

Take *Discain Project Services v Opecprime Development Ltd* where the adjudicator discussed aspects of the case in the presence of one party without notifying the other. HHJ Bowsher QC

held that the adjudicator had an obligation to adhere to the rules of natural justice and that hearing one party in the absence of the other was a serious breach of those rules, so enforcement of the adjudicator's award could be validly resisted. His actions gave the appearance of bias.

Now, that seems to me to be a very restrictive view of fairness. Many people had thought that because the adjudicator was expected to get to grips with the case quickly by talking to the parties separately, if he did so, no one would regard his actions as suggesting bias.

Then, more recently, a similar issue arose in *Balfour Beatty Construction Ltd v The Mayor and Burgess of the London Borough of Lambeth*. In that case, the claimant in a dispute as to delay on a project produced a programme and analysis that the adjudicator considered to be inadequate. Therefore, the adjudicator prepared his own critical path analysis. On an application to enforce the adjudicator's decision the defendant claimed that there had been a breach of natural justice because he had not had the opportunity to comment on that analysis.

Anyway, the defendant succeeded. It was held that although the adjudicator was entitled to take the initiative in ascertaining the facts and the law, he had gone too far in this case. In the first place, the defendant had not had an opportunity to confront the evidence. And, in the second place, by constructing the claimant's case for him the adjudicator gave the appearance of bias.

Judge Lloyd did accept that *"the purpose of adjudication is not to be thwarted by an overly sensitive concern for procedural niceties"*, and that *"adjudication is necessarily crude in resolution of disputes"*, but said that a serious breach of natural justice would nevertheless invalidate a decision.

And perhaps the most interesting thing about this decision is its clear policy statement. Judge LLOYD tells us in clear terms where the courts are going on adjudication. He says:

“It is now clear that the Construction Industry regards adjudication not simply as a staging post toward the final resolution of the dispute in arbitration or litigation but as having itself considerable weight and impact that in practice goes beyond the legal requirement that the decision has for the time being to be observed. Lack of impartiality or of fairness in adjudication must be seen in that light.”

So, what we seem to be seeing is a move away from the quick and dirty approach that many people inevitably thought that adjudication was going to comprise. I remember, for example, that when I did the TeCSA adjudication course in the early days, the received wisdom was that the adjudicator should expect to contact the parties independently so as to glean as much information as possible, as quickly as possible. But, in the light of these cases, that approach is plainly wrong. The new wisdom appears to be that adjudication is being used for very large cases; not just small simple cases brought by sub-contractors.

Also, it is comparatively unusual for adjudicators' decisions to be taken on to litigation or arbitration. So, because of the increasing significance of adjudication to the Industry, the courts, as a matter of public policy, are ensuring that the process is as rigorously fair as is possible within the confines of the time constraints that apply.

My own view is that that policy is probably correct. The courts are trying to get the balance right between the need for speed and certainty on the one hand, and the right decision on the other. As Judge LLOYD said in *Balfour Beatty*, the adjudicator does not have to apply natural

justice with the same precision as an arbitrator. But he must act with sufficient procedural fairness for the parties to have confidence in the system.

However, the downside is that these decisions do breed a degree of uncertainty. Because it is all a matter of balance, it is difficult to know just how much natural justice you are entitled to get, and there is a danger that adjudicators will become overcautious and spend so much time worrying about being fair that they won't be able to concentrate fully on getting at the facts of the case.

Or it might lead adjudicators to resign rather than form decisions on complicated cases where they don't feel they have time to proceed in accordance with all the paraphernalia of natural justice. Though that in itself raises difficult questions because, unless the Scheme for Construction Contracts or similar rules apply, the basis upon which an adjudicator may resign is itself uncertain.

Conclusion

In conclusion, I think, by and large, that adjudication has assisted the cause of fairness in dispute resolution. If there is gross error then the dispute can be reopened in litigation or arbitration. And the judges have sought to ensure that a reasonable degree of procedural rigour is applied by adjudicators so as to minimise the potential for such errors.

The necessarily rough and ready nature of adjudication has the ability to cause injustices, but it's probably better than the pre-existing state of dispute resolution in construction – which gives the lie to those who said: *“Reform? Aren't things bad enough already?”*

In our seventh Seminar, **Jeremy Glover** outlined the courts' responses to attempts by parties to evade adjudicators' decisions.

Avoiding An Adjudicator's Decision

Unsurprisingly, a number of attempts have been made to set-off against sums awarded by adjudicators. There have been a number of decisions which have suggested that it might just be possible to do this.

The first Court of Appeal decision

One case involved one of our fellow speakers, HHJ Kirkham. In *Parsons Plastics (Research & Development) Ltd v Purac Ltd*¹, Parsons had been successful in an ad-hoc adjudication carried out in accordance with the terms of the sub-contract and not pursuant to the HGCRA.

Six days after the adjudicator's decision was given and before paying any money pursuant to that decision, Purac served a withholding notice pursuant to that sub-contract. Purac claimed that having taken over the sub-contract works pursuant to clause 20(c), they were entitled to deduct from monies otherwise due to Parsons the reasonable cost of completing the works. Purac had paid £303,000 plus VAT to a second sub-contractor to complete the work. That was a larger sum than the sum awarded by the adjudicator.

The Court of Appeal², agreeing with the judge, held that under the terms of this particular contract it was indeed open to Purac to set-off against the adjudicator's decision any other claim they had against Parsons, as long as that claim had not been determined by the adjudicator. The relevant clause of this particular sub-contract stated that:

"31. Nothing contained in this Deed whether expressly or by incorporation or by implication shall in any way restrict [Purac's] equitable or common law rights of set-off. Without prejudice to the generality of the foregoing, [Purac] shall have the right to set off against any sum due to [Parsons] whether hereunder or otherwise a fair and reasonable sum in respect of or on account of any claim or claims that have been made or which are to be made against [Purac] by the Purchaser the subject matter of which touches or concerns the Sub-Contract Works."

Accordingly, Lord Justice Pill said:

"It is open to the respondents to set off against the adjudicator's decision any other claim they have against the appellants which had not been determined by the adjudicator. The adjudicator's decision cannot be re-litigated in other proceedings but, on the wording of this sub-contract, can be made subject to set-off and counterclaim."

The attitude of the TCC to HGCRA adjudications

In cases which did involve the HGCRA, an apparent difference of opinion emerged within the judges of the TCC. The first case to consider the relevant principles governing set-off and withholding from an adjudicator's decision was the decision of HHJ Hicks QC in *VHE Construction PLC v RBSTB Trust Co Ltd*³, who said:

"I conclude that enforcement proceedings such as these are proceedings to enforce a contractual obligation, namely the obligation to comply with the decision. The decision does not have the status of a judgment . . ."

"There is, however, a question whether the obligation to 'comply with' a decision which requires the payment of a sum of money has any greater effect than to make that sum a simple debt, for example by excluding certain defences which could be raised in answer to an action on such a debt . . ."

¹ 13 August 2001 – unreported

² (2002) CILL 1868

³ (2000) CILL 1592

HHJ Hicks QC, having considered whether the contractual payment provisions that had been relied on by the paying party gave the adjudicator's decision the status of a simple debt or went as far as to exclude defences such as set-off, concluded:

"It would make a nonsense of the overall purpose of . . . the Act . . . if payments required to comply with adjudication decisions were more vulnerable to attack in this way than those simply falling due under the ordinary contractual machinery . . . therefore, I find these compelling reasons for concluding that . . . at least on the facts of this case, 'comply' means 'comply, without recourse to defences or cross-claims not raised in the adjudication'."

In another case, *Solland Interiors v Daraydan International*⁴, a different judge, HHJ Seymour QC, followed *VHE* and said that where there were two separate contracts you could not set off a claim for liquidated damages under a related contract, which exceeded the total amount awarded in an adjudication under a separate contract. The fact that there were apparently other disputes between the parties did not constitute any reason not to enter judgment for the sums awarded by the adjudicator.

The parties had entered into a contract, which said that the decision of an adjudicator was binding pending final determination by the court. There was no provision in that particular contract to set off or deduct against that award. HHJ Seymour QC said:

"The parties plainly intended that any decision of an adjudicator should be 'binding'. It seems to me that inherent in the concept of a decision being 'binding' is, first, that the parties should accept the decision for the period for which the Conditions provided, and, second, that the parties should give effect to it. Giving effect to a decision that A should pay £X to B means that A pays £X to B, and

not that A pays some different sum or no sum at all. Any other construction of clause 22(5) of the Conditions would mean that in the Building Contract adjudication was simply for fun and could not be for profit."

However, in the case of *KNS Industrial Services (Birmingham) Ltd v Sindall Ltd*⁵, HHJ Lloyd QC held that rights of set-off were not excluded under the HGCR. The contract required compliance with an adjudicator's decision without prejudice to other rights under the contract.

"Therefore other rights under the contract which were not the subject of the decision remain available to the relevant party. If therefore by the time an adjudicator makes a decision requiring payment by a party, the contract has been lawfully terminated by that party (or that party has real prospects of success in supporting that termination) or some other event has occurred which under the contract entitles a party not to pay then the amount required to be paid by the decision does not have to be paid."

In a further decision, *David Mclean Housing Contractors Ltd v Swansea Housing Association Ltd*⁶, HHJ Lloyd QC had to consider a situation where the paying party had paid up following an adjudicator's decision everything save for an amount in respect of liquidated damages which reflected the adjudicator's view about the extension of time that was sought by the claimant. The defendant alleged that it had given an effective notice of withholding in respect of these damages in accordance with the terms of the contract. HHJ Lloyd QC said:

". . . in my view the defendant has realistic prospects of success in maintaining that it gave an effective notice, particularly having regard to the fact that underlying all this was the fact that all along it had made it very clear that it wanted to recover liquidated damages. It had served its notices . . . it would be manifestly unjust also to deprive the defendant of an opportunity of

⁴ (2002) 83 Con LR 109

⁵ (2001) 75 Con LR 71

⁶ (2002) CILL 1811

maintaining that it was not obliged to pay the full amount of the adjudicator's decision."

The situation came to a head following two decisions late last year in the TCC, *Bovis Lend Lease Ltd v Triangle Developments Ltd*⁷, and *Levolux AT Ltd v Ferson Contractors Ltd*.⁸

In *Bovis*, HHJ Thornton QC had to consider whether a party could withhold against a sum directed to be paid by an adjudicator following three adjudications between the parties. The judge concluded by setting out a number of factors that must be in place before such a withholding can be made:

- The decision of an adjudicator that money must be paid gives rise to a separate contractual obligation. The paying party must comply with that decision within the stipulated period. Usually the paying party cannot withhold, make a deduction, set-off or cross-claim against that sum.
- To withhold against an adjudicator's decision, an effective notice to withhold payment must usually have been given prior to the adjudication notice being given and being ruled upon and made part of the subject matter of that decision.
- However, if there are other contractual terms which clearly have the effect of superseding, or providing for an entitlement to avoid or deduct from, a payment directed to be paid by an adjudicator's decision, those terms will prevail.
- Equally, where a paying party is given an entitlement to deduct from or cross-claim against the sum directed to be paid as a result of the

same, or another, adjudication decision, the first decision will not be enforced or, alternatively, judgment will be stayed.

The contract here included a clause which said that:

"In the event of the determination . . . and so long as that employment has not been reinstated then . . . the provisions of this contract which require any further payment or release of retention to Bovis shall not apply".

Triangle had determined Bovis' contract for failing to proceed regularly and diligently, and the judge found that it was entitled to rely on both the contract and the adjudicator's third decision (that the determination was valid) to withhold payment of the sum directed to be paid under the adjudicator's first decision. Bovis' contention (namely that the determination of its employment was invalid) was not sufficient, in the absence of either an adjudicator's decision to that effect or, alternatively, any sufficient evidence to sustain that contention, to enable them to counter this.

It should be stressed that HHJ Thornton QC did not see that there was any contradiction in the way the judges of the TCC had been approaching this question. For example, of HHJ Lloyd QC's decision in *Mclean v Swansea*, he said:

" . . . David Mclean was a case where the court was giving effect to and complying with a further decision of the adjudicator as to extensions of time and their corollary, the extent of delayed completion by the receiving party and its entitlement to liquidated damages for delay. It was for that reason that effect was not given to the separate decision in favour of the paying party that a sum of money was due to it."

⁷ (2003) CILL 1939

⁸ 26/6/02 – unreported

The Court of Appeal takes charge – the Levolux decision

Earlier, HHJ Wilcox had come to a slightly different conclusion in *Levolux v Ferson*⁹, and it was with this case that the situation was clarified by the Court of Appeal. Here, Levolux referred a dispute to adjudication in respect of a failure to pay application number two. Ferson relied upon a notice of withholding payment, but Levolux contended that the notice was not a valid notice within section 111 of the Act. The adjudicator held that the withholding notice did not comply with the requirements for section 111 of the HGCRA.

When the matter came before the court, Ferson's primary case was that it had determined the sub-contract. In these circumstances, Ferson relied on clause 29.8 of the sub-contract:

"If the Contractor shall determine the Sub-Contract for any reason mentioned in Clause 29.6, [including wrongful suspension of work] the following provisions shall apply:-

(1) All sums of money that may then be due or accruing due from the Contractor to the Sub-Contractor will cease to be due or to accrue due;"

Alternatively, Ferson argued that it could rely upon the amended clause and set-off and/or counter-claim against the decision of the adjudicator. The amendment to the GC/Works sub-contract stated, at clause 38A.11, that *"neither party shall be precluded from raising any right of set-off, counterclaim or abatement in connection with the enforcement of an Adjudicator's decision"*. Levolux had suspended the works as a result of non-payment. Ferson then issued determination notices for failing to proceed regularly and diligently. The dispute referred to adjudication was in

respect of the valuation and withholding, and did not include an issue in respect of determination.

HHJ Wilcox held that the amount owing pursuant to the decision should be paid. This was on the basis that the parties had accepted, by reference to clause 38A.7 of the contract, that a decision would be binding pending litigation or arbitration.

Notwithstanding that the amended clause 38A.11 in respect of a right to withhold and/or set-off against an adjudicator's decision was in conflict with section 111 of the HGCRA requiring an effective notice, HHJ Wilcox held that the necessary implication of the adjudicator's award was that Levolux had been entitled to suspend the works and accordingly that the purported determination based upon wrongful suspension had no contractual effect. Clause 29.8 did not apply to monies due under an adjudicator's award provided always that the adjudicator had not exceeded his jurisdiction. There was no suggestion in this case that the adjudicator had not acted within his jurisdiction.

Ferson appealed. Lord Justice Mantell succinctly summarised the point at issue in the fourth paragraph of his judgment:

"A central issue in the appeal is whether, pending final resolution by arbitration or litigation, an adjudicator's decision should be enforced in derogation of contractual rights with which it may conflict."

Ferson, of course, relied on the third limb of HHJ Thornton QC's conclusions in the *Bovis v Triangle* case:

"... where other contractual terms clearly have the effect of superseding, or provide for an entitlement to avoid or deduct from a payment directed to be paid by an adjudicator's decision, those terms will prevail."

⁹ (2003) CILL 1956

However, Lord Justice Mantell disagreed:

“... to my mind the answer to this appeal is the straightforward one provided by Judge Wilcox. The intended purpose of s. 108 is plain. It is explained in those cases to which I have referred in an earlier part of this judgment. If Mr Collings and His Honour Judge Thornton are right, that purpose would be defeated. The contract must be construed so as to give effect to the intention of Parliament rather than to defeat it. If that cannot be achieved by way of construction, then the offending clause must be struck down. I would suggest that it can be done without the need to strike out any particular clause and that is by the means adopted by Judge Wilcox. Clauses 29.8 and 29.9 must be read as not applying to monies due by reason of an adjudicator’s decision.”

The language used is reminiscent of the simple straightforward approach of Mr Justice Dyson in *Macob* and the Court of Appeal in *Bouygues*. Thus the situation is clear, you cannot get round an adjudicator’s decision by adopting any set-offs or counter-claims.¹⁰ Where there is any (potential) conflict between the rights of the contract and an adjudicator’s decision, it is the adjudicator’s decision that will prevail. That was the intention of Parliament. Of course, if the adjudicator had been given the jurisdiction to consider whether the determination of *Levolux* had been valid, the situation may well have been different. If you want to challenge that decision, you can, but only because an adjudicator’s decision is only binding on a temporary basis.

So what can you do?

Rely on your own adjudication and not the court’s.

If you want to raise a set-off or counter-claim and it cannot be part of an

adjudication commenced by another party, consider whether you can launch your own adjudication. If successful you will have a decision you can use to reduce any exposure. However, you should act quickly as the case of *Sir Robert McAlpine v Pring & St Hill Ltd*¹¹ (unreported) demonstrates.

Here, HHJ Moseley QC had to consider whether to enforce an adjudicator’s decision where the defendant said that it had a set-off against the claimant which exceeded the sum awarded in the adjudication and that in the time between the hearing and the giving of the judgment, a period of some 10 days, the defendant had set in motion an adjudication with a view to resolving the question of that set-off.

In reaching his decision, HHJ Moseley QC first had to consider the question of set-off. He, in a decision that would have found favour with the Court of Appeal in *Levolux*¹², held that there was a provision in the contract for a final date for payment: the adjudication was in accordance with the contract and the adjudicator ordered that payment be made within seven days. That was, in the judge’s view, the final date for payment.

The judge then considered whether to grant a stay of execution for the four to six weeks it would take to reach a decision in the second adjudication. He decided not to:

“Mr Evans’s final fallback position was then that I ought to grant a stay until the adjudication decision on the final payment is forthcoming. That adjudication is expected between four and six weeks hence. In my view, I ought not to grant a stay... the claimant is entitled to judgment. As a general principle, when the person is entitled to have a sum of

¹⁰ A similar situation prevails in Scotland. See the decision of Lord Young in *A v B*, 17 December 2002.

¹¹ Unreported – 2 October 2001

¹² Incidentally, both of these cases involved the construction of a *brise-soleil*

money paid to him under a judgment, that sum of money should be paid and no stay ought to be imposed. I decline to grant the stay . . .”

Conclusion

Following *Bouygues* the attitude of the Court of Appeal seemed clear. *Levolux* has provided confirmation. Adjudication is the creation of Parliament. Parliament has created something which is new and different and which provides for swift summary justice. The Court of Appeal has recognised that on occasion this may lead to an injustice. However, that has not stopped the Court of Appeal from enforcing apparently unjust decisions in the past and it is unlikely to stop the Court of Appeal from doing so in the future. Thus it is becoming increasingly more difficult to find ways round an adjudicator’s decision, even if you consider that it is a bad one.

www.adjudication.co.uk

There will undoubtedly be further challenges made to the adjudication legislation over the next year. For this reason, Fenwick Elliott continue to be one of the backers of this premier free adjudication website. If you log on you will find not only full up-to-date details (including, where possible, transcripts) of the latest reported decisions, but also practical assistance on all aspects of the adjudication process.

It is also possible to request the appointment of an adjudicator from the site. The cost of doing so is £250 including VAT, which makes it cheaper than many of ANB’s. In addition, the appointment fee will be part of the adjudicator’s fees and so there is no need to pay this up front.

If you have any comments, either contact ***Chris Hough*** or fill in the feedback form on the site.

5. THE EFFECT OF TIME BEING AT LARGE

When parties are negotiating the key terms of a contract, one of the major issues they have to consider is the date for completion. As ***Anna Roberts*** discusses, a failure to meet a completion date can have serious consequences for either or both parties. It is for this reason that contracts often allow for extensions of time to be granted and liquidated damages to be paid in the event of delay.

When agreeing the terms of a contract, thought must be given to the date specified for completion; the remedies available to both parties if one party causes a delay which affects the progress of the works which prevents completion by the completion date; and the contractual mechanism for dealing with such delays.

It is always advisable to deal with these issues at the time when the contract is agreed. Sometimes, however, situations arise where the date for completion is not prescribed or, perhaps, the employer has caused a delay and is not allowed by the contract to grant an extension of time. When does this happen?

Letters of intent

It can be that in a simple form of contract, the parties simply omit to include terms as to completion or the incorporation of a mechanism for the award of an extension of time. This can often be the case when the parties are operating pursuant to a letter of intent, in the hope that a formal contract will be finalised. In a letter of intent, it is not uncommon for the parties to specify a completion date or a contract period but fail to incorporate an extension of time mechanism, instead hoping to rely on the mechanism contained in the formal contract that is intended to supersede the letter of intent.

In these circumstances and where the formal contract is not then agreed, the effect of the omission is that there is no way in which time can be extended to reflect any delays caused by any act or omission on the part of the employer. Accordingly, the ordering of extra work, or the failure to give access, would constitute an act of prevention which means that the contractor cannot complete by the agreed dates.

What happens then, in terms of when the contract works are to be completed and how will this affect a contractor?

Completion time "at large"

The answer to this first question is that time for completion becomes "at large".

Contractors and lawyers alike tend towards the conclusion that, where an employer causes a delay and cannot or does not award the appropriate extension of time, then the original completion obligations cease to be valid, but are replaced by an obligation on the part of the contractor to complete the works within a reasonable time. Some weight is lent to this conclusion by the Supply of Goods and Services Act 1982, section 14, which provides:

"where, under a contract for the supply of a service by a supplier acting in the course of the business, the time for the service to be carried out is not fixed by the contract, left to be fixed in a manner agreed by the contract or determined by the course of dealing between the parties, there is an implied term that the supplier will carry out the service within a reasonable time."

This is all very well but does not deal with the case in hand, that is, where a contractual completion date ceases to constitute the contractor's obligation as to time.

Peak v McKinney and *British Steel Corporation v Cleveland Bridge and Engineering Co. Ltd* are often cited as authority for the proposition that an obligation to complete within a reasonable time replaces the original time for completion. These cases do not necessarily go so far as to say this. The courts have not provided a definitive answer; however, that, for the time being, is the interpretation given.

A reasonable time for completion

This being the case, what constitutes a reasonable time for completion? The general rule can be found in *Hick v Raymond and Reid* in which the court made clear that a contractor "fulfils his obligation, notwithstanding protracted delay, so long as such delay is attributable to causes beyond his control, and he has acted neither negligently nor unreasonably".

This analysis is not particularly helpful to a contractor defending a claim for unliquidated damages where an employer argues that the works have to be completed within a reasonable time.

So how does a contractor set about providing what constitutes a reasonable time?

For example, what does "causes beyond his control" mean? In *Scott Lithgow Ltd v Secretary of State for Defence*, the employer agreed to pay to the contractor his delay costs due to "alterations, suspensions of work or any other cause beyond the Contractor's control". The court held that a quality failure on the part of a nominated sub-contractor which led to delay was a cause beyond the contractor's control. It is arguable that the reasoning applied by the court would apply equally to domestic sub-contractors or suppliers. This is because the matter was approached in terms of whether or

not, as a matter of fact, the contractor was able to supervise the work being carried out effectively so that the quality of the product was assured. It would not have been enough that the contractor was deemed to have responsibility for the sub-contractor's work by virtue of a contractual relationship.

While this is good news for the contractor, can it really be what the court intended? It seems sensible that this should be the case with nominated sub-contractors where the employer has a contractual relationship with the sub-contractor but what about in the case of a domestic sub-contractor or supplier? The employer has no recourse against that sub-contractor or supplier, unlike the main contractor. It therefore seems strange that this risk should be borne by the employer. Although the court may, in the future, clarify this point, for the time being it is likely that a cause "beyond the contractor's control" includes failures on the part of a nominated or domestic sub-contractor or supplier. This concept is, in many ways, analogous to the issue of what constitutes a reasonable time. As seen above, the contractor fulfils his completion obligations if the delays he suffered were attributable to causes beyond his control.

When should "reasonable time" be assessed?

What is clear is the point in time at which a reasonable time should be assessed. It has been held that what constitutes a reasonable time can only be decided after the work has been done.

The way the court will assess what constitutes a reasonable time was outlined in *British Steel Corporation v Cleveland Bridge*, in which Goff J said: "*I have first to consider what would, in ordinary circumstances, be reasonable time for the performance of the relevant services; and I*

have then to consider to what extent the time for performance by BSC [the contractor] was in fact extended by extraordinary circumstances outside their Control."

On this basis, it seems that in assessing what constitutes a reasonable time, a contractor should look at the initial reasonable time for completion (which may be the original completion date) and then add on an appropriate amount of time for each event that affects completion which is outside his control.

Going forward then, what is the effect on the contractor of an obligation to complete within a reasonable time?

The concept of "time at large" has its origins as a defence to a claim for liquidated damages. Where an employer prevents a contractor from completing the works by the contractual completion date and for some reason the contract either does not contain an extension of time mechanism or that mechanism fails because, for example, time is at large, the employer loses its right to claim liquidated damages for late completion.

If the employer wants to claim damages for delay, its remedy will be in general damages. It will have to show that the works were not completed within a reasonable time and will have to prove its actual losses. In addition, the employer will have to demonstrate that its losses were caused by the failure of the contractor to complete within a reasonable time. The contractor will be liable for those losses that are attributable to any period of time which is beyond that deemed to be reasonable.

There is an argument that in this type of situation, the general damages are subject to a cap, being the level of liquidated damages prescribed by the contract, if liquidated damages are set by the contract. There is no decided case on this

point within the English jurisdiction but this view is the preferred view of the textbook writers.

Conclusion

If the contract does not provide for a completion date or that date is lost, for whatever reason, it is probably the position that the contractor's obligation is to complete within a reasonable time. When the works are complete, the parties can assess what constitutes a reasonable date for the completion of the works and, in this assessment, the contractor will have the benefit of delays that were a result of causes beyond his control. When a reasonable date has been established, the employer may claim general damages incurred as a result of delays beyond that date. These damages may be subject to a cap, being the amount of liquidated damages that would otherwise have been recoverable under the contract for that delay.

6 GETTING PAID

Always a thorny topic, *Jon Miller* sets out some of the difficulties you might face and also some of the ways round those difficulties. We have held a number of in-house seminars based on the difficulties often faced when attempting to get paid. If you would like further details please contact either Jon Miller or Jeremy Glover.

Property in materials

Fixed materials

When materials are fixed to the land, the property passes to the landowner. This principle stretches back to Roman law in order to prevent the needless demolition of buildings. Believe it or not there are cases where a builder has worked on another's land by mistake and the landowner stood back and accepted the benefit without telling the builder. The

landowner in these circumstances has to pay compensation¹³.

In an attempt to get round this, some contracts have elaborate retention of title clauses where, once materials have been fixed to the land and property has passed to the landowner, the supplier can "trace" the value of the materials into the landowner's bank account and the landowner then has an obligation to put these funds into a separate account etcetera, for the benefit of the suppliers.

It is very difficult for the court to uphold such a provision as:-

- the contract may not even be with the landowner and he is not party to the contract;
- the landowner may not put the monies in a separate account, even if he has signed a contract to say that he would do so;
- there is a possibility that the clause may operate as a charge on the landowner's bank account. The charge against the company is invalid for want of registration under the Companies Act.

Meaning of fixture

In view of this rule, it becomes very important to identify when materials are fixed to the land. If the materials are attached to the land even in a minimal way, the burden of proof shifts to the supplier to show that they are not fixed and that he has retained property. Unfortunately, each case depends on its own facts, but it has been held that:-

"something as basic as doors, windows and shutters, in the construction of a building are so much part of the structure

¹³ *Ramsden v Dyson*

that it would [be unreal]to suggest that the joinery did not become a fixture.”¹⁴

Accordingly, if ceiling panels are easily removable they probably do not become fixed to the land, but the frame which is attached to the ceiling is probably a fixture.

Overall, it is very difficult to retain property and materials when they are fixed to the land. I recommend that your contract state clearly:-

- property and materials only pass on payment;
- if they are fixed to the land then the employer shall put the funds in a separate bank account representing the value of the materials in your name.

However, I doubt the employer will actually put the funds in a separate account and I have grave doubts that this will be upheld by the court. At best this gives you a negotiating position.

Unfixed materials

A supplier’s right to repossess unfixed materials depends on the terms of the supply contract. If the contract is for sale of goods (i.e. supply only) the customer can take ownership of the materials without paying for them and pass them on to another purchaser. This is because under section 25 of the Sale of Goods Act 1979:-

“where a person having brought or agreed to buy goods obtains, with the consent of the seller, possession of the goods . . . delivery or transfer by that person (the purchaser) . . . of the goods . . . under any sale, pledge or other disposition thereof, to any person [the sub-purchaser] receiving the same in good faith and without notice of . . . right of the original

seller in respect of the goods . . .” transfers title to the sub-purchaser.

In *Archivent v Strathclyde General Council*¹⁵ a supplier entered into a contract with the contractor for the first time. The supplier’s normal policy was to ask for cash before delivery but this was overlooked.

The court found that section 25 of the Sale of Goods Act 1979 applied and title/property to even the unfixed goods had passed to the employer under the contract between the employer and the contractor, as the employer had no notice of the retention of title clause in the supply contract.

Work and materials contract

Section 25 of the Sale of Goods Act does not apply to contracts for work and material. In *Dawber Williamson v Humberside County Council*¹⁶, the sub-contractor supplied slates to a contractor who went into liquidation before paying for them. None of the slates had been fixed. The employer sought to argue on section 25 of the Sale of Goods Act but he failed as this was a contract for work and materials, whereas the Sale of Goods Act applied only to contract of sale or just materials.

The position for unfixed materials in work and materials contracts is unclear. Most contracts now specifically deal with the position. According to JCT 1998 clause 16.1:-

“Unfixed materials and goods delivered to, placed on or adjacent to the Works . . . shall not be removed except for use upon the Works unless the architect has consented in writing . . . Where a value of any such materials or goods has . . . been included in any Interim Certificate . . . [and] has been paid by the

¹⁴ *Minshaw v Lloyd* 1837 2 M&W 450

¹⁵ 1984 27 BLR

¹⁶ 1979 14 BLR 70

Employer, such materials and goods shall become the property of the Employer.”

Accordingly, under the JCT 1998 arrangement, unfixed materials and goods cannot be removed from site without the consent of the architect. If the contractor removes the goods, he is in breach of contract and the liquidator may sue him for damages which the employer suffers as a result.

Significantly, if the employer pays for the unfixed goods, they become the employer's property.

Advice

I would include a term in all your contracts for work and materials that property/title in goods does not transfer to the customer until you have received payment.

If a supplier retains title in unfixed materials, then he should have a contract with the owner of the land to re-enter and take the materials, otherwise the landowner can simply refuse entry onto the site. Possession tends to be nine-tenths of the law.

Late Payment of Commercial Debts (Interest) Act 1998

Interest payable on all contracts

The Act applies to all contracts for supply of goods and services between business and public authorities entered into after 7 August 2002. The Act imposes a right to interest – if there is no term in the contract awarding interest, the Act implies its own term.

Parties to a contract can agree their own method of compensation for late payment – this may or may not be interest. If they do have their own method of compensation, this must be a “substantial

remedy”. If the contract does not contain a “substantial remedy”, interest is payable at 8 per cent over base rate.

Statutory interest starts to accrue the day after the final date for payment until judgment is made in favour of the suppliers. The sum on which interest is calculated is inclusive of VAT, but the interest sum itself is exclusive of VAT.

There are no cases yet on what is a “substantial remedy”. Nevertheless, most construction contracts award a rate of interest which is 5 per cent over base rate, rather than 8 per cent over base rate which the Act suggests – see for example clause 30.1.1.1 of the JCT 1998 Edition.

Retention

Protecting retention

Retention is a key feature of the construction and engineering industry. Essentially, the employer will retain 3 or 5 per cent paying half of practical completion, and the remaining half once all the defects in the works have been corrected and the defects liability period expires.

Key points to remember with retention are:-

- It should be a term of the contract that the retention fund should be put in a separate account in the name of the contractor/sub-contractor. The reason for this is simple. If the customer goes into liquidation and the retention is mixed in with the customer's funds, then there is no way in which the liquidator will know which are the customer's funds and which are the contractor's retention. The liquidator will take all the money.

- Allowing your funds to be mixed in with the customer's means that you could have a charge (see earlier) over the customer's bank account. A charge against a company can be invalid for want of registration. According to the JCT 1998 form of contract, the contractor can ask for the retention to be put into a separate account, and the employer must comply with this request¹⁷. It is surprising how many contractors forget to ask until the employer is in financial difficulty.
- The employer's interest in the retention should be fiduciary as trustee for the contractor. Essentially, this arrangement tries to re-enforce the position that the contractor does not own the retention fund, he merely holds it as trustee for the ultimate owner and beneficiary, the employer.

Failure to include a requirement that the employer's interest is as "fiduciary/trustee" is not fatal, but it is always best to include such an obligation.

The JCT 1998 form of contract includes the following rules of retention:-

*"... the Employer's interest in the Retention is fiduciary as trustee for the Contractor and for any Nominated Sub-Contractor (without obligation to invest)."*¹⁸

*"The Employer shall ... if the Contractor ... so requests, at the date of payment under each Interim Certificate place the Retention in a separate banking account (so designated to identify the amount as the Retention ...)."*¹⁹

Note that under the JCT form of contract, the contractor is to request the retention be put in a separate account with each

Interim Certificate. If the final date for payment of the retention has passed, and the employer has failed to pay the retention, bear in mind that the employer should have served a Withholding Notice under the Housing Grants Act – this requirement is explicitly set out in clause 30.5.4 of the JCT 1998 form of contract.

Termination and suspension

Failure to pay does not allow a party to terminate.

A failure to pay a debt which is due and payable is very unlikely to allow the supplier to terminate a building contract²⁰. It has been held that *"The appointment [of administrative receivers] may be consistent with the firm intention to continue with the contract rather than to abandon it, especially if it is profitable"*.²¹

Insolvency events

In order to get around this problem, many Standard Form Contracts list a series of insolvency events which allow a party to terminate.

This may be a "formal" insolvency, such as having an administrative receiver or liquidator appointed. Alternatively, it may just be that being "unable to pay debts" is sufficient grounds under the contract to terminate.

What is clear, however, is that without an expressed right to terminate in insolvency situations, you are probably unlikely to have the right to bring the contract to an end and will have to continue for a while with little prospect of being paid.

¹⁷ Clause 30.5.3

¹⁸ Clause 30.5.1

¹⁹ Clause 30.5.3

²⁰ *Decro – Wall International v Practitioners in Marketing* 1971 2AER 216

²¹ *Laing and Morrison Knudson v Aegon Insurance* 1997 86 BLR 70

ACE Conditions/JCT 1998

The ACE Conditions allow termination:-

- “if circumstances arise for which the Consultant is not responsible and which he considers make it irresponsible for him to perform all or any part of the Services.”²²

I am not sure whether the customer’s insolvency would make it irresponsible for the consultant to comply²³;

- “in the event of the failure of the client to make any payment properly due to the consultant.”

Under JCT 1998, if the employer does not:-

- “pay by the final date for payment the amount properly due to the Contractor”²⁴;
- “does not give access to the site”²⁵;
- “or commits an act of insolvency (as defined by the Contract)”²⁶;

the contractor can serve a notice determining the contract.

Suspension under the Housing Grants Act

The Housing Grants Act applies to contracts for construction operations evidenced in writing. The Act states that where a sum is not paid in full by the final date for payment, and no effective withholding notice has been given, the supplier can suspend performance of his obligations. The supplier has to first give 7 days’ notice of his intention to suspend stating the grounds on which it is intended to suspend.

²² Clause 5.3

²³ Clause 5.4

²⁴ Clause 28.2.1.1

²⁵ Clause 28.2.2.4

²⁶ Clause 28.2.4

This applies to all contracts whether or not it is set out in the contract form. Most standard forms simply reiterate this right.

Procedure

The procedure for terminating a contract varies from one agreement to another. It is absolutely vital that you follow this procedure strictly to the letter. If you do not terminate in accordance with the terms set out in the contract, then you will be in breach of contract enabling the employer to claim damages against you.

According to the JCT 1998 Edition, if the employer:-

- does not pay by the final date for payment the amount properly due to the Contractor; or
- interferes or obstructs with the issue of any certificate, etc.²⁷;

the contractor may give to the employer a notice specifying the default or defaults.

If the default continues for 14 days from receipt of the notice, then the contractor may at the end of the 14-day period, or within 10 days from the expiry of the 14-day period, serve a further notice determining its employment.

The significant points to bear in mind here are:-

- A notice must be given in writing by actual delivery, special delivery or recorded delivery²⁸. Sending it by post is not sufficient.
- If sent by special delivery or recorded delivery, the notice shall be deemed to have been received 48 hours after

²⁷ Clause 28.2 – this gives a long list of employer default events

²⁸ Clause 28.1

the date of posting (excluding Saturday and Sunday and public holidays). Accordingly, when you are working out when the 14 days fall, you need to work out when the notice is deemed to have been served.

- The first notice to be served must specify the default or defaults.
- 14 days after receipt of the first notice, the contractor may determine his employment. If he does not do it on day 14, he has only 10 days thereafter in which to determine his employment.

Under a termination in accordance with clause 5.3 of the ACE Conditions, 2 weeks' notice needs to be given. However, notices under the ACE Conditions are to be sent by fax or first class post at the address shown in the contract. They take effect when they have been received by the client or the consultant "*as the case may be*"²⁹.

Getting it wrong

The consequences of getting a suspension or termination wrong can be very serious.

If you attempt to terminate the contract not in accordance with its terms, the employer may be entitled to allege that you have breached the contract, and recover (significant) damages from you. The employer can recover the additional costs of completing the works, and some of the additional costs or losses he incurs as a result of the delay.

Determination/suspension can have a very powerful affect on a party who is not paying, but in my view it should not be done without a decision being taken at the highest level, and forensic examination of the contract terms is needed

²⁹ Clause 10.1

7. HEALTH AND SAFETY

In recent years, the UK Construction Industry has seen an ever-increasing crackdown by the Health and Safety Executive and the Government on workplace safety, most recently focusing on the reduction of falls from height on construction sites. *Leigh Child* examines these latest developments.

Since 2000, the Government Health and Safety Commission (HSC) has been targeting construction-site accidents and falls from height as part of a bigger initiative to reduce workplace fatalities and major injuries with its *Revitalising Health and Safety Campaign*. The Campaign aims not only to raise awareness of workplace safety but also to see improvements in the number of work-related illnesses and absences resulting from unsafe working practices. In addition, the ongoing European-led HSE initiative "*Don't Fall for It*", promoted in conjunction with ECA, Amicus-AEEU and UCATT, aims to educate the industry and reduce the number of construction-site fatalities and major injuries.

As part of the initiative, the HSE carried out a record number of inspections during a site blitz in June of this year. A second round of inspections is planned for September. This will focus on the improper use of scaffolding and ladders, the main causes of falls on construction sites.

Consideration of the unacceptably high occurrence of construction-site fatalities and major injuries reveals why the HSE is determined to improve construction safety. In 1999, there were 26 construction-site deaths attributable to falls from height. In 2000–1 falls from height resulting in death accounted for 44 per cent of all construction accidents reported that year and by 2001–2 that figure had grown 47 per cent with 37

deaths. The Construction Industry has recognised this and in 2001 set itself the long-term objective of reducing the rate of fatalities and major injuries by 40 per cent by 2004/5 and by 60 per cent by 2009/10³⁰. This is no mean feat when there have already been 12 deaths on construction sites in 2003 by April. Improper use of scaffolding and ladders is cited as the main cause of falls on construction sites.

Under the Health and Safety at Work Act 1974 (HSWA), the HSE has the power to prosecute a company or its individual officers for failure to ensure the health and safety of its employees. Since January this year, a total of 66 successful prosecutions resulting in fines totalling £740,800 under HSWA have already been made against the construction industry. The average fine this year stands at £10,427³¹. This figure, however, does not take into account the legal costs that are incurred by a company involved in a health and safety prosecution. These can often add up to a few thousand pounds even in the most straightforward cases.

In addition to prosecution under the HSWA, companies need to remain mindful of the Construction (Health, Safety and Welfare) Regulations 1996 which, amongst other activities, regulate prevention of falls from height. There have been 60 successful prosecutions under these Regulations in the first half of this year.

It is not just the construction companies and the workers on site that need to be involved in creating a safer work environment. This is an issue that needs to be recognised and addressed from

³⁰ At the Construction Safety Summit

³¹ All figures as at 9 May 2003. This figure is slightly higher due to two high profile cases resulting in death of one or more employees and attracting fines of £75,000 and £175,000 respectively.

inception of a building design. The HSE are concerned that many designers and planning supervisors show little concern for designing out working at height where possible. This is perhaps surprising in light of the legal duty imposed under Construction (Design and Management) Regulations 1994 (CDMs). Although prosecutions under these Regulations appear less frequent (there have only been nine so far this year), the average fine is almost double that under the HSWA³².

The combined fiscal implications of breaching health and safety legislation for the industry should not be underestimated. The addition of the fines received for the 1994 and 1996 Regulations, along with miscellaneous other Regulations under which successful prosecutions have been brought³³, pushes the total health and safety bill for the construction industry in the first half of 2003 to £1,000,000.

Aside from the legislative duties imposed on construction companies, do not forget that a charge of corporate manslaughter may be brought for an accident resulting from a breach of health and safety. Currently, this offence is infamously hard to prove owing to the requirement of successfully proving negligence on the part of a “controlling mind” within the company. Most commonly, this is taken to mean that the gross negligence of a director of the company was directly causative to the accident. The recent attempt to prosecute key personnel at Balfour Beatty and Railtrack under corporate manslaughter and health and safety charges could, if successful, have huge implications on the Construction

³² As at 9 May 2003 the average fine under the 1994 Regulations stood at £24,800 and under the 1996 Regulations it stood at £1,732.08.

³³ Such as: Gas Safety (Installation and Use) Regulations 1998, The Management of Health and Safety at Work Regulations 1999, Lifting Operations, Lifting Equipment Regulations 1998, and Provision and Use of Work Equipment Regulations 1998.

Industry. There is also the oft-heard criticism that smaller firms tend to suffer a disadvantage under such an offence, as it is easier to trace a line of responsibility through a company of 10 employees as opposed to one with hundreds. It is claimed the proposed statutory offence of corporate killing will address this imbalance. The draft bill will focus on the prosecution of companies – something many feel may be inadequate in making directors and those with real responsibility more aware of the importance of health and safety. However, directors may still be personally liable to a charge of manslaughter and offences under HSWA if it can be shown that management failure is the cause or one of the major causes of a death.

The offence will carry no maximum fine penalty and the level of the fine may be used to have a deterrent effect. There is even pressure from some sources to impose custodial sentences on key players in companies. Criticisms levelled at the new offence range from it encouraging a risk-averse environment in the Construction Industry to the increase in insurance premiums at a time when the construction market can ill afford it.

Of course, whether the HSE brings an action or not, it is always open to the family of an employee to bring a civil action against a company for negligence.

In light of the above penalties and with the upcoming site inspection blitz planned for September 2003, construction companies would do well to carry out a pre-emptive review of their health and safety conditions.

It is becoming common practice for companies to engage external health and safety consultants to advise on the adequacy of health and safety practices. The consultants can work with the company to develop a comprehensive

health and safety policy, which can be implemented effectively. It is slowly being recognised that the mere existence of a health and safety policy will often fall far short of the mark and that the key is thorough implementation of such policy through employee training, constant monitoring and continuing development of supervisor and employee safety awareness.

In the worst case scenario of an accident having already occurred on site, early consideration should be given to whether a change in practice is required to prevent a repeat incident and any such changes implemented – without intervention from the HSE. Therefore, should the HSE investigate an accident the company can be seen to have been proactive rather than reactive in the area of health and safety. It will always stand a company in good stead to be well prepared for an HSE investigation, and view it as an opportunity to explain the situation and put forward evidence that all had been done to make the site a safe place to work. Full cooperation with the HSE will always be viewed favourably by a court should a trial take place.

Prevention is always better than a cure.

8. CASE ROUND-UP

Our usual case round-up comes from three different sources.

Tony Francis, together with John Denis-Smith, continues to edit the *Construction Industry Law Letter* (CILL). CILL is published by Informa Professional. For further information on subscribing to the *Construction Industry Law Letter*, please contact Eleanor Slade by telephone on +44 (0) 20 7017 4017 or by email: eleanor.slade@informa.com.

Tony Francis and Nicholas Gould produce a weekly legal briefing for the

Building magazine website. Log on to www.building.co.uk for further details.

Finally there is our monthly bulletin, entitled *Dispatch*, which is available in hard copy or electronic form, and has now been running for over two years. This summarises the recent legal and other relevant developments. If you would like to look at recent editions, please go to www.fenwickelliott.co.uk. If you would like to receive a copy every month, please contact Jeremy Glover.

We have split the case round-up into two, and deal first with summaries of some of the most recent adjudication cases, which are taken from *Dispatch*. Then we set out some of the more important case summaries, starting with one from the *Building* website and then continuing with further cases from CILL. An index appears at the end of this review.

ADJUDICATION

Beck Peppiatt Ltd v Norwest Holst Construction Ltd

This decision of Mr Justice Forbes provides further guidance on the question of what constitutes a dispute. It also provides an example of a claimant, rather than proceeding with an adjudication, actively seeking a declaration from the courts that the adjudicator had no jurisdiction before the adjudicator had the chance to make a decision.

Mr Justice Forbes quoted with approval the words of HHJ LLOYD QC in *Sindall v Solland*:-

"For there to be a dispute for the purposes of exercising the statutory right to adjudication it must be clear that a point has emerged from the process of discussion or negotiation that has ended and that there is something which needs to be decided."

He approached the *Beck* case on the basis of these words and further held that he did not see any conflict between this approach and the approach of the Court of Appeal in *Halki v Sopex* (see also *Cowlin v CFW*). Here, on reviewing the facts of the case, Mr Justice Forbes concluded it was clear that, before the notice of adjudication was served, the process of discussion and negotiation had ended and that something was needed to be decided, namely the correct position with regard to the outstanding items on the final account.

This was notwithstanding that some two and a half weeks before the adjudication began, Norwest Holst had served 11 lever arch files of documentation on Beck. Beck had suggested that they had not been given sufficient time to consider the files before the adjudication began. However, the judge looked at the factual context as a whole. The 11 files largely consisted of information which Beck had seen before. The files were also a response to Beck's position and were sufficient in themselves to give rise to a dispute since the serving of the files had thereby served to reject that position.

Carillion Construction Ltd v Devonport Royal Dockyard Ltd

HHJ Bowsher QC had to consider an application for the enforcement of an adjudication decision where the sum involved was some £7,451,320 plus VAT. Devonport alleged that the adjudicator did not have jurisdiction because the relevant contract was not (evidenced) in writing and that no dispute had arisen prior to the service of the notice of adjudication.

The key to the first argument was whether the project was cost reimbursable. As this was a material term, following the CA decision in *RJT Consulting v DM Engineering*, that term must have been evidenced in writing for the dispute to be referable to adjudication. Here, for the

purposes of the case it was agreed that there was a construction agreement in writing, but what was at issue was an alleged oral agreement that radically changed the written agreement. The change was far greater than a typical variation made pursuant to the terms of a construction contract. Therefore the adjudicator did not have jurisdiction.

The Construction Centre Group Ltd v Highland Council

Lord MacFadyen had to consider a dispute arising in relation to the Small Isles and Inverie Ferry scheme. The defenders resisted payment of an adjudicator's decision in the sum of £250k.

By clause 66 of the contract, the parties had to give "*effect forthwith to every decision of . . . the Adjudicator on a dispute given under this clause*" unless that decision was revised by agreement or the dispute had been referred to arbitration and an arbitral award had been made. The Highland Council argued that the effect of awarding summary judgment would be to give a final judgment in place of an interim decision. Lord MacFadyen disagreed, saying that not to allow enforcement would obstruct the purpose of section 108 of the HGCR. One of the points of adjudication was to obtain payment on a provisional basis. CCGL were not asking the court to endorse the soundness of the adjudicator's decision but were asking the court to recognise that the parties had committed themselves contractually to implement that decision.

The Highland Council also argued that as they had a claim against CCGL for the payment of liquidated damages (quantified at a sum in excess of £250k), they were entitled to refuse to pay the sum awarded. A valid notice had been served in pursuant to section 111 of the HGCR. CCGL argued that as the liquidated

damages claim could have been advanced before the adjudicator, the Highland Council could not rely on it now to resist enforcement. Further, CCGL submitted that section 111 referred to notices in relation to payment certificates and not to notices in respect of adjudicators' decisions.

Lord MacFadyen held that as the Highland Council had chosen not to advance their retention argument before the adjudicator, they could not rely upon it now. That said, the right of retention was not lost and that right remained against any future sum which might fall due to CCGL under the contract. However, there had been nothing to prevent the Highland Council from putting forward their claim for liquidated damages in the adjudication. It was now too late. Section 111 was not intended to permit the giving of a withholding notice in respect of an adjudicator's award.

Lord MacFadyen concluded that:

"it would . . . be destructive of the effectiveness of the institution of adjudication if a responding party could decline to put forward an available defence in the course of the adjudication, then give a section 111 notice seeking to withhold on that ground the sum awarded by the Adjudicator."

Cowlin Construction Ltd v CFW Architects

CFW resisted enforcement on the grounds that the adjudicator did not have jurisdiction because there was no construction contract between the parties and/or that there was no dispute capable of being referred to adjudication.

In a previous adjudication, the adjudicator had decided on the form of contract entered into between the parties. In the adjudication which was the subject of this case, the second adjudicator applied that contract and decided that CFW should

pay Cowlin the sum of £275,211.51 plus VAT. Cowlin said that the decision by the first adjudicator on the contract was binding. CFW had initially accepted that the first adjudicator had jurisdiction to decide the contract position and had issued a counter notice, they then changed their mind. However, HHJ Kirkham found that CFW had submitted to jurisdiction in the first adjudication. When they did this, they had been represented by solicitors. Even though CFW had swiftly changed their position, this was not sufficient.

CFW then said that they (and their insurers) had not had sufficient opportunity to consider the issues referred to the adjudicator and hence there was no dispute. On 3 May 2002, when Cowlin made a peremptory demand which required a substantive response by 17 May, CFW had already been in possession of the claim since 27 February and further details since 11 March – some 8 weeks. Therefore the judge, adopting the *Halki v Solpex* analysis, concluded that CFW should have known broadly whether they admitted some or all of Cowlin's claim or rejected it totally. Thus they had had sufficient opportunity to indicate their response. By not responding to the ultimatum in these circumstances, a dispute had arisen.

Debeck v T&E

HHJ Kirkham applied the CA decision in *RJT Consulting Engineers Ltd v DM Engineering Ltd* in deciding that for an oral agreement to fall within section 107 of the HGCRA, all the relevant terms of the agreement must be clearly recorded in writing. Debeck had applied for summary judgment arguing amongst other things that the contract was a construction contract falling within the HGCRA and that in the absence of any section 110 or section 111 notices, summary judgment should be granted.

Although there was a fax from Debeck which it said contained all the relevant terms of the agreement, the judge rejected this argument for two reasons. The fax did not set out or record all of those matters on which Debeck itself had relied upon in pursuing its claim. For example, the fax did not explain even in summary terms the scope of the work (or the programming and sequencing) to be undertaken. Equally, it was unclear from the fax whether materials were to be supplied or not. In addition, a director of T&E gave evidence that there were further terms of the contract between the parties which were not recorded in the fax. These included references to the quality of the work and the time within which the work was to be undertaken.

Thus, HHJ Kirkham concluded that Debeck could not rely upon the fax to bring the oral agreement within section 107. A claimant cannot cherry-pick and identify those parts of an agreement upon which it relies and ignore matters which the defendant says were agreed between the parties. The judge suggested that one way for a party to obtain the benefit of the HGCRA, would be for that party to seek to clarify the terms which it believes have been orally agreed and invite the other contracting party to agree that those are indeed the terms of the agreement.

Deko Scotland Ltd v ERJV & others

ERJV was set up to design and construct a new royal infirmary and medical school. The plasterboard and partitioning sub-contractor went into liquidation and the sub-contract was novated to Deko who assumed all of the responsibilities and liabilities under the sub-contract. A dispute arose and an adjudicator issued a decision. The adjudication was governed by an amended version of the ORSA Adjudication Rules 1998 version 1.2.

When the matter came to court, the only point in issue was the adjudicator's power to make an award in respect of the costs and expenses of the adjudication. One of the amendments introduced a new clause, 21A, providing that *"the Adjudicator may require any Party to pay or make contribution to, the legal costs of another Party arising in the Adjudication . . ."* The adjudicator ordered ERJV to pay half of Deko's costs including Deko's legal costs. Deko had claimed costs in the following five categories: claims consultant, surveyor, solicitors, internal costs and one half of the adjudicator's fee.

Lord Drummond Young held that the adjudicator did have the power by virtue of amended clause 21A to decide that ERJV should pay half of Deko's costs. However, that power was limited to Deko's legal costs only. Further, these legal costs were liable to taxation and the same principles as those that applied to the legal expenses of litigation (and arbitration) applied. Thus that part of the adjudicator's decision dealing with costs would not be enforced until those legal costs had been assessed by the court or agreed between the parties.

This case was decided in accordance with an amended version of the old TeCSA rules. The current rules adopt a different approach, providing that an adjudicator only has jurisdiction to award costs if the parties agree. The new version of the rules goes further, stating that regardless of the terms of the contract, the adjudicator shall have no power to require the party that referred the dispute to adjudication to pay the costs of the other party merely by reason of having referred the dispute to adjudication.

Levolux AT Ltd v Ferson Contractors Ltd

This was a CA case. The key issue was whether, pending final resolution by

arbitration or litigation, an adjudicator's decision should be enforced notwithstanding that it might conflict with the contractual rights of the parties. In other words, could a "paying party" use, for example, determination provisions to get round an adjudication decision.

In the present case, clause 29.8 of the contract provided that if the contractor shall determine the sub-contract for any reason mentioned in clause 29.6 then all sums of money that may then be due or accruing due from the contractor to the sub-contractor shall cease to be due or accrue. Whilst clause 29.9 provided that until after completion of the sub-contract works and the making good of defects, the contractor shall not be bound by any provisions of the sub-contract to make any further payment to the sub-contractor.

Ferson claimed that the terms of the contract overrode the obligation to make payment in accordance with the adjudicator's decision. The CA disagreed emphatically with this proposition and, agreeing with HHJ Wilcox, dismissed the appeal. LJ Mantell said:-

"But to my mind the answer to this appeal is the straightforward one provided by Judge Wilcox. The intended purpose of s. 108 is plain . . . The contract must be construed so as to give effect to the intention of Parliament rather than to defeat it."

The intention of Parliament according to LJ Longmore:-

". . . was to avoid just the kind of arguments to which we have listened in the present case."

Further, by clause 38A.9 the parties agreed, regardless of clause 38B which provided for the right to refer disputes to arbitration, to comply forthwith with any decision of the adjudicator, and to submit to summary enforcement in respect of all such decisions. Thus, the parties had

agreed not only that the adjudication was binding but also that they would comply with any adjudication notwithstanding the arbitration clause. This clause prevented the losing party from applying for a stay and required that party to submit to an application for summary judgment.

Orange EBS Ltd v ABB Ltd

In the decision of *Beck v Norwest Holst*, Forbes J had to consider whether or not there was a dispute. Forbes J said that the CA decision in *Halki v Sopex* was fully binding but further added that the law in this regard had been satisfactorily stated by HHJ Lloyd QC in the decision in *Sindall v Solland*. Here, HHJ Kirkham applied both principles in deciding that a dispute had arisen. However, it was clearly a close call.

Part of the dispute related to the final account. Orange submitted a final account on 2 December 2002, but served a notice of adjudication on 6 January 2003. Orange's contract had been terminated in July, but it had taken no further steps between July and December. ABB instructed an investigator to consider the final account and suggested they would be able to respond by 20 January and if no agreement had been reached within 7 days thereafter ABB indicated that they were willing to submit to adjudication.

ABB also said that there could be no dispute because the contractual machinery under DOM/1 had not run its course before the notice of adjudication was served. Orange said that the effect of repudiation was to bring the sub-contract to an end and thus the contractual mechanism no longer existed. HHJ Kirkham agreed. Once the sub-contract was terminated, the contractual mechanism for payment also fell away.

Applying the *Halki* test, the fact that the ABB had not admitted the claim or paid,

meant that a dispute had arisen. Applying the *Sindall v Solland* test was more difficult. HHJ Kirkham had to decide whether, when the adjudication notice was served, the process of discussion and/or negotiation had ended and whether there was something which needed to be decided. Given the industry Christmas shutdown and the fact that ABB had made what they thought was a reasonable alternative suggestion in relation to the timetable, it was submitted that it would be "bizarre, unreasonable, absurd and unworkable to conclude that a dispute had arisen".

However, on balance, the judge concluded that by 6 January 2003, sufficient time had elapsed for ABB to have both evaluated the claim and to have concluded any discussions and/or negotiations with Orange. This was notwithstanding the holiday period. The process of negotiation and discussion had concluded and so a dispute had arisen.

OTHER CASES

Building Magazine Legal Briefing

“No Records, No Claim”

Attorney-General for the Falkland Islands v Gordon Forbes Construction (Falklands) Limited (NO2),

The case

This was an application by the Attorney-General for the Falkland Islands for the determination of a preliminary point of law in arbitration proceedings. Gordon Forbes and the Government entered into a FIDIC fourth edition contract in 1997 to carry out some building works. A dispute arose which was referred to arbitration. Clause 53.4 of the FIDIC conditions required such claims to be verified by contemporary records. Gordon Forbes wanted to introduce witness statements

into the arbitration covering those parts of the claim where no such contemporary records existed. The arbitrator refused an application by the Attorney-General inviting the arbitrator to rule on the meaning of “contemporary records”, and also the extent to which witness statements could be used to cover the lack of such records.

The issue

The issue for determination was whether on the true meaning of clause 53 of the FIDIC conditions witness statements could be introduced into evidence to supplement contemporary records.

The decision

Acting Judge Sanders held that “contemporary records” in the FIDIC conditions meant original or primary documents or copies produced or prepared on or about the time giving rise to the claim. These documents could be produced by either the contractor or the employer. However, it was held that contemporary records did not mean witness statements that were produced long after the event. As a result, where there were no such contemporary records in support of a claim, that claim must fail. Witness statements could only be used to identify or clarify contemporary records but not substitute them.

Comment

Clause 53 of the FIDIC conditions deals with procedures for claims, and requires a contractor to give notice of claim to the engineer (with a copy to the) within 28 days of the event arising. It is not unusual for notices to be sent late, or indeed not to be sent at all. Contractors often bring claims long after the event, and often a failure to serve notices is not fatal to contractor claims.

However, clause 53 requires the contractor to keep contemporary records in order to support the claim. It seems clear that a failure to keep those contemporary records will effectively mean that the contractor is unable to support his claim and that the claim will fail. The case emphasises the need not only to give notice at the time of the claim, but also, and perhaps more importantly, to ensure that contemporary records are kept in support of the claim.

Construction Industry Law Letter

BHP Billiton Petroleum Ltd and others v Dalmine SpA

Court of Appeal

Lord Justice Aldous Lord Justice Kay and Lord Justice Rix

Judgment delivered 19 February 2003

The facts

Dalmine manufactured and provided 12? diameter steel pipes used in the construction of a sub-sea gas re-injection pipeline serving the oil and gas fields in the Liverpool Bay area of the Irish Sea.

The pipeline was laid in 1994 but did not enter service until April 1996. On 7 June 1996, gas bubbles were noticed on the surface of the sea. By 22 June 1996, leaks had been identified at six failure sites. It was established not only that the pipeline had failed at each of the leak sites but also that it had not failed elsewhere. Cracks had developed in the roots of welds which joined the pipes together, had propagated from the weld roots into the parent metal of the adjacent pipe, and had developed into through-wall cracks, linking the interior and exterior walls of the pipe. The cracks had initiated because of a combination of excessive hardness of the weld root metal and because the pipeline was subject, as was expected, to sour service conditions, i.e. the

combination of hydrogen sulphide and water.

At the hearing, the only live issue concerned causation. Dalmine contended that, even if the pipe had been compliant, it would have failed.

BHP accepted that it bore the burden of proving that the incorporation of non-compliant pipe caused the pipeline to fail, but submitted that Dalmine bore the burden of proving that the pipeline would have failed in any event, i.e. even if it had been made solely of compliant pipe.

At first instance, Cresswell J found for BHP. Dalmine appealed. The question for the Court of Appeal was whether the burden of proof concerning Dalmine's contention rested on it or upon BHP.

Issues and findings

On whom did the burden of proof lie where the defendants alleged that even if the pipes had been compliant, they would nonetheless have failed?

On the defendant who raised the issue. In most cases the pleadings will be a good guide to where the burden lies.

Commentary

Although clearly a sensible direction on the facts of the case, the reasoning of the Court of Appeal in support of the judgment may raise problems in future cases. Not all claims in court proceedings, let alone arbitration or adjudication, are well pleaded, so letting the matter rest largely on those pleadings may be an uncertain guide.

Given the extended consideration which the court gave to the "but for" test and issues of causation, it appears that they themselves felt that the pleadings are not the only basis upon which this question is

to be determined. But resort to the law on causation is not itself necessarily a clear guide either in every case.

The court referred to and approved the Court of Appeal decision in *Chester v Afshar* (CILL 2002 1886). That decision was not, however, made only on grounds of a logical analysis of causation itself, but involved an explicit assertion of public policy considerations as a ground for deciding causation issues in a given way. These might indicate the answer in a clinical negligence case but be less helpful in a construction scenario.

Co-operative Insurance Society Ltd v Henry Boot Scotland Ltd and others

Technology and Construction Court
His Honour Judge Richard Seymour QC
Judgment delivered 2 July 2002

The facts

CIS and Boot contracted for the demolition, design and reconstruction of a building in Glasgow. The terms were the JCT Standard Form of Building Contract, 1980 edition as amended. The CDP element included various earthworks and sub-structure works. There was, however, no document in which were set out either the Contractors' Proposals or the CDP Analysis.

Clause 2.1.2 provided that: "*For the purpose of so carrying out and completing the works the contractor shall . . . complete the design for the contractor's designed portion . . . and the contractor shall comply with the directions which the architect/the contract administrator shall give for the integration of the design for the contractor's designed portion with the design/or the works as a whole, subject to the provisions of cl. 2.7.*"

Clause 2.2.4 provided that: "*The contractor shall be deemed to have inspected and examined the site and its surroundings and to have satisfied himself before*

submitting his tender as to the form and nature of the site including the ground and subsoil.”

Clause 2.7.1 provided that: *“Insofar as the design of the contractor’s designed portion is comprised in the contractor’s proposals and in what the contractor is to complete under cl 2.1.2, and in accordance with the employer’s requirements and the conditions (including any further design which has to be carried out by the contractor as a result of a variation), the contractor shall have in respect of any defect or insufficiency in such design the like liability to the employer, whether under statute or otherwise, as would an architect or, as the case may be, other appropriate professional designer holding himself out as competent to take on work for such design who, acting independently under a separate contract with the employer, had supplied such design for or in connection with works to be carried out and completed by a building contractor not being the supplier of the design.”*

Warranties in the Appendix included 8.1.4 which said: *“... if defects or possible defects of design which would be apparent to an experienced and competent contractor shall be revealed, the contractor shall, notwithstanding that neither the contractor nor any sub-contractor . . . shall be responsible for the element of design in point, report such defects or possible defects to the architect or the employer . . .”*

During the execution of the works, water and soil flooded into sub-basement excavations. One of CIS’s claims, made against both Boot and CIS’s design consultants (the third defendant), related to the alleged consequences of that occurrence.

The court heard various preliminary issues. Boot argued that the contract documents included a site investigation report by Terra Tek, which was referred to in a contract drawing, and that its obligations with respect to the design of works was limited to producing more

detailed drawings of the design already specified by CIS’s consultants.

Issues and findings

Was the report on ground conditions referred to in a contract drawing thereby made a contract document?

No, nor was there any representation that the ground conditions would correspond to those indicated in the report.

Was Boot’s design obligation limited to producing detailed drawings of the design?

No, the obligation involved taking over responsibility for that design, however fully developed it had been at the time of contract.

Commentary

The judge’s finding as to the extent of a contractor’s design responsibility under a JCT WCD arrangement is of significance. Whilst the judge acknowledges that the contractor’s obligation is only to complete the design, the interpretation of what this entails effectively amounts to an adoption of the design insofar as prepared by the design team.

It is not unusual for an employer to retain a consultant to carry out site investigations prior to entering into a contract. As in this case, the fact that the employer may release to a contractor the results of such an investigation does not necessarily translate into any assumption of risk, particularly where there is, as is common, a provision deeming the contractor to have carried out his own investigations.

E Clarke & Son (Coaches) Ltd v ACT Construction Ltd

Court of Appeal
Lord Justice Ward, Lord Justice Laws,
Lord Justice Keene
Judgment delivered 16 July 2002

The facts

At the request of the appellant, the respondent carried out design and construction works to convert existing premises into a coach depot. The parties did not enter into formal terms and a payment was made by the appellant following applications made from time to time by the respondent. The respondent left the site in 1994 and subsequently commenced proceedings claiming £208,000 in unpaid fees. The respondent contended that the appellant had agreed that it was to be paid on a time and materials basis. The appellant contended that payment was to be inclusive and capped at £815,000. The appellant counter-claimed an overpayment and damages for defective work.

Judge Thornton was called upon to decide a number of preliminary issues. Judge Thornton found that no contract came into being, as neither price nor scope had been agreed between the parties with any precision. Accordingly, the respondent was entitled to be paid on a *quantum meruit* basis. Following a further hearing, Judge Thornton awarded the respondent £186,000. The appellant appealed.

Issues and findings

Was there a contract?

Yes, even if there was no entire contract, there could still be an agreement to carry out the work albeit that the scope and price was not agreed. Provided there was an instruction to do work and an

acceptance of that instruction then there would be a contract.

What were the payment terms?

There was a “contractual *quantum meruit*”. A term would be implied into the contract requiring that a reasonable sum be paid for the work done.

Commentary

The scenario described by Ward LJ where work is carried out on the basis of an instruction without an agreement as to price or work scope is not uncommon. On the facts of this case, Ward LJ held that whilst an entire contract had not come into existence, a contract had nevertheless still come into being notwithstanding the absence of agreement on a number of essential terms.

It is this finding that could prove to be of real significance. It is rare for work to be carried out in the absence of an initiating request and on the basis of this decision, assuming work is carried out pursuant to a request, then this could give rise to a contract remaining to be either subsequently agreed or, failing agreement implied. Subject to evidence in writing, it should be remembered that the very existence of a contract of this nature may constitute a construction contract for the purposes of the HGCRA 1996.

Impresa Castelli SpA v Cola Holdings Ltd

Technology and Construction Court
His Honour Judge Thornton QC
Judgment delivered 2 May 2002

The facts

Impresa contracted with Cola to construct a hotel on terms incorporating the 1981 JCT With Contractor’s Design Standard Form of Building Contract.

The project suffered delay and there were a series of agreements, the first in February 1999, providing for a new date for completion. The second agreement in September 1999 provided for stage provision of parts of the hotel so that access would be allowed to the hotel to enable it to fully operate as a hotel and the claimant was to complete the development as soon as possible. The second agreement provided that nothing in it was to amount to practical completion for the purposes of the original agreement and the revised date for completion was not altered.

There followed a third meeting between the parties concerned with whether practical completion had occurred, the final account and liquidated damages. The meeting was preceded by Impresa giving details of its variation account dealing with the cost of all variations which had been ordered and led to the third and final variation agreement, the October agreement. As at the date of that agreement, Impresa had not formulated nor advanced a claim for loss and expense, but the existence of a claim was apparently known to both parties.

The relevant terms of the October agreement were as follows:

“Whereas: (i) This agreement is made pursuant to . . . the construction contract . . . which is deemed to be incorporated herein (save as varied below) as if set out in full with regard to the design and construction of a hotel . . .

(ii) The parties hereto have agreed to settle outstanding claims pursuant to the construction contract and have agreed a sum of money to be paid for the works carried out by the contractor.

(iii) Save where provided otherwise in this agreement words and terms herein shall have the same definitions as have been assigned to them in the construction contract.

1. The parties agree that the final value in respect of works carried out by the contractor in accordance with the Bills of Quantities and the issued drawings, and in respect of the works to be carried out under the construction contract, including for the avoidance of doubt the fitness centre is £11,450,000 plus VAT. For the avoidance of doubt the cost of any extra specified after 12 October 1999 will be in addition to this amount.

2. The said sum shall be paid and accepted in full and final mutual settlement of both parties’ existing claims pursuant to or connected with the construction contract or the works to which it relates, excluding the employer’s right to claim for any defective works which may become apparent after the date hereof. . .

8. The other terms and provisions contained in the construction contract shall remain in full force and effect save as specifically varied herein . . .”

Disputes arose, amongst them whether or not the effect of the grant of access under the September agreement amounted to the defendant taking partial possession such that liquidated damages were thenceforth not recoverable by the defendant and whether the effect of the October agreement was to settle any claim by the claimant for loss and expense.

Issues and findings

Under JCT 1981 With Contractor’s Design, where the parties agreed that the employer would be given access to the works for the purposes of operating them as a hotel, did that amount to the taking of partial possession under clause 17.1.4 of the conditions of contract?

No, on the true construction of the various agreements under which access was provided to the employer, such access was properly to be treated as use or occupation under clause 23.3.2 of the contract. Thus, partial possession had not

occurred and the liability of the contractor in respect of liquidated damages was unaffected by the grant of such access.

Did the October agreement settle any claim by the claimant in respect of loss and expense?

No, the claim for loss and expense was to be contrasted with a Final Account claim. Only the latter had been settled.

Commentary

It is not unusual for an employer to wish to make use of a commercial property before work on it is complete. This case illustrates the importance to such an employer of ensuring that taking such access is not to be treated as taking partial possession of the works, with the consequential loss of the right to liquidated damages.

The judge's decision on the second issue reported here may at first sight be surprising. An observer might have considered that the aim of the parties as businessmen negotiating the October agreement was to settle all matters between the parties. Nonetheless, the objective meaning of (and not subjective intention behind) the agreement is to be given effect and the judgment emphasises the contract between a claim under a contract in respect of the value of work done and a claim for loss and expense. It is worth noting in the context of crystallisation of disputes in an adjudication context that the judge held that a claim for loss and expense is not to be treated as having been made before it is advanced under the contract conditions.

Jeancharm Ltd v Barnet FC Ltd

Court of Appeal (Civil Division)
Lord Justice Peter Gibson, Lord Justice Keene, Mr Justice Jacob
Judgment delivered 16 January 2003

The facts

By an agreement made in 1998, Jeancharm agreed to supply Barnet with football kit for the seasons 1999–2000 and 2000–1. Clauses 3 and 4 provided:

“3.1 All orders from the club must be in the form of a written purchase order, authorised by the chairman, and all invoices that are matched to such orders will be settled within 45 days from the invoice date.

“Payments will be made by the club within 45 days, having deducted any relevant penalty clauses or credit notes that are due.

“Payment of a correct invoice, more than 45 days after the invoice date, shall incur interest at the rate of 5% per week (pro rata) on the outstanding sum, for the period from 45 days after the invoice date.

“4 ... Training gear deliveries

If the training kit referred to in cl. 3 is delivered after the due date of 14 June, unless otherwise agreed in writing then the club will be entitled to a late penalty payment of 20p per garment per day.

“Club shop replica items

Within 45 days of the date of an official purchase order from the club unless otherwise agreed in writing if Beaver has not supplied the complete order, the club reserves the right on the part of the order not delivered to receive a penalty for late delivery at the rate of 20p per garment per day.

“Club shop leisurewear items

Within eight weeks of the date of an official order from the club, unless otherwise agreed in writing, if Beaver has not supplied the complete order, the club reserves the right on the part of the order not delivered to receive a penalty for late delivery at the rate of 20p per garment per day.”

Thus, if Barnet was late in paying, it had to pay interest at 5 per cent per week. If Jeancharm delivered late, it had to pay 20p per garment per day. At court Barnet argued that clause 3 was unenforceable as a penalty. At first instance, the court held

that the clause was not a penalty and hence was not unenforceable. Therefore, although Barnet was liable for a principal sum of around £5,142, it was liable for around £15,000 more by way of interest. Jeancharm appealed successfully to the Court of Appeal.

Issues and findings

What is the test for determining whether a clause is a penalty?

The test is as set out in *Dunlop v New Garage*. The Privy Council judgment in *Phillips Hong King Ltd v The Attorney-General of Hong Kong* (1993) 61 BLR 41 had not modified that test.

Was clause 3 a penalty?

Yes, the interest rate specified amounted to 260 per cent per year. That went beyond any loss, which Jeancharm had identified as contemplated by the clause. The clause was therefore unenforceable.

Commentary

Payment of interest on late payments is of course now required by statute. Since the statute requires contracts to provide for such interest to be higher than the current lending rates, they may be considered to constitute a form of penalty permitted by Parliament. However, provision for levying of interest (or other sums) going beyond that may well amount to an unenforceable penalty.

The court's emphatic statement that the Privy Council in *Phillips Hong Kong Ltd v The Attorney-General of Hong Kong* does not represent any change in the test in *Dunlop v New Garage* is, however, of potentially greater importance.

Middlesbrough Football & Athletic Company (1986) Ltd v Liverpool Football & Athletic Grounds Plc

Court of Appeal

Lord Justice Simon Brown, Lord Justice May and Lord Justice Clarke

Judgment delivered 25 November 2002

The facts

In the summer of 1999, Middlesbrough bought Christian Ziege from AC Milan for approximately £4m. In the summer of 2000, Liverpool bought him for £5.5m, a transaction to which Middlesbrough were strongly opposed and which Liverpool achieved, Middlesbrough alleged, only by breaking the Football Association Premier League Rules ("the Rules"). The Rules are contractually binding on all member clubs of the Premier League and on all players.

The Rules provided *inter alia*:

"1. A club shall be at liberty at any time to make an approach to a player with a view to negotiating a contract with such a player:

1.2 in a case of a contract player, with the prior written consent of the club . . . to which he is contracted . . .

22. A contract between a club and a player shall be treated as confidential and its contents shall not be disclosed or divulged either directly or indirectly to any person, firm or company . . . except:

22.1 with the prior written permission of both parties . . ."

Ziege had secured the inclusion, within his contract with Middlesbrough, of the following clause:

"f7. In the event that during the period of this contract, Middlesbrough receive an offer in writing for the transfer of the player for a minimum of £5.5m, the club will give the player permission to discuss terms with the offering club. If the player agrees terms with the offering club, Middlesbrough will grant

his release and terminate his contract on receipt of a written request from the player.”

Liverpool had identified in their team “a particular weakness on the left side” and wanted to “sign a left-sided player with attacking qualities”. In May 2000, they came to learn of cl f7 in Ziege’s contract. In the event, some days prior to 24 July 2000, Liverpool approached Ziege directly without informing Middlesbrough of their interest, and, having persuaded him to agree to move, they made a written offer that he be transferred at that price, which then occurred.

But for Liverpool’s breaches of the Rules, Middlesbrough argued that Ziege would either have remained with them or, had Liverpool or any other club bought his registration, they would have paid substantially more than the £5.5m in fact paid. Either way, Middlesbrough suffered loss. Middlesbrough claimed on the basis that they could have sold Ziege for more than £5.5m or alternatively, that, had he stayed, the team would have performed significantly better in the next season thus avoiding many of the losses they in fact suffered that year.

Liverpool sought to strike out the claim on the basis that they would never have paid more than £5.5m, and Ziege could not have been sold for more than that. Alternatively, Middlesbrough could not show that it would have achieved a better result in the season 2000–1. Master Eyre refused that application, but Mr Justice Anstell allowed Liverpool’s appeal. Middlesbrough appealed to the Court of Appeal who allowed that appeal, thus restoring Middlesbrough’s action.

Issues and findings

Was the judge correct to have considered Middlesbrough’s claim as too speculative to found a claim in damages?

No, on the balance of probabilities, Middlesbrough would be likely to demonstrate Liverpool’s breach of the Rules. Damages can be assessed on a loss of chance basis, and the fact that they might be difficult to ascertain was not a ground to refuse recovery.

Commentary

Football is inherently a risky business, but even so, difficulties in ascertaining damages for a breach of contract (which was the substance of this case) are not a reason to refuse to grant them. This is of course also the case of construction contracts where claims, for example in respect of lost contribution to overheads or wasted management costs, are often more easy to formulate than quantify.

In such cases, it is all too easy to dismiss a claim as being too speculative. However, while the complainant will of course have to satisfy evidential requirements, the Court of Appeal has re-emphasised the principle that a tribunal must not abdicate its responsibility to ascertain damages, even where it is hard to do so.

Motherwell Bridge Construction Ltd (t/a Motherwell Bridge Storage Tanks) v Micafil Vakuumtechnik and another

Technology and Construction Court
His Honour Judge Toulmin QC CMG
Judgment delivered 31 January 2002

The facts

Micafil awarded MBST two sub-contracts on FIDIC terms to construct an autoclave. MBST brought claims amongst other things alleging critical delay was caused by Micafil, and seeking sums on the basis that, in the absence of an award of an appropriate extension of time, it had to carry out accelerated working, the cost of which it claimed from Micafil.

In respect of the acceleration, MBST sought the cost of working night shifts from 19 June to 11 September 1998 in order to try to keep up to schedule as a result of the fact, they alleged, that they had to do substantial additional work owing to Micafil's changes in design over what was originally envisaged in the contract. MBST claimed that since they incurred these costs in attempting to comply with Micafil's wish for the contract to be kept to time and against the background of Micafil's refusal to grant appropriate extensions of time, they were entitled to be paid for the work which they did in trying to accelerate the work to keep up with the schedule.

Issues and findings

How should delay be assessed?

The crucial questions were (i) was the delay on the critical path; and (ii) if so, was it caused by the claimant? On the evidence, the delays were on the critical path but were not the fault of the claimant. Therefore the claimant was entitled to claim for prolongation costs, and the defendant would not recover any liquidated damages.

Was the claimant entitled to sums in respect of acceleration, which it carried out to avoid the imposition of liquidated damages?

Yes.

Commentary

Questions of delay analysis have been the subject of much debate and the decision in *Henry Boot v Malmaison* itself gave rise to discussion in legal circles. In expressly adopting the formulation in that case, HHJ Toulmin QC CMG provides welcome confirmation that the courts are seeking to adopt a consistent approach. The award of acceleration costs suggests

that, where a party is wrongly refused an extension of time and then accelerates its work to avoid liquidated damages, then it may be entitled to recover those costs even in the absence of any agreement with the employer. Such a concept is well known in the US (as "constructive acceleration") but its recognition here will be of great assistance to contractors faced with the unreasonable conduct of the employer or contract administrator.

OTV Birwelco Ltd v Technical & General Guarantee Company Ltd

Technology and Construction Court
His Honour Judge Thornton QC
Judgment delivered 20 September 2002

The facts

OTV entered into a contract with Northwest Water for the provision of a waste treatment plant. OTV engaged Woodbank as sub-contractor for the electrical installation. As a condition of the sub-contract Woodbank provided a bond to a value of £41,153 or 10% of the sub-contract sum. The bond, dated 8 July 1997, was provided by T&G and included the following condition:

"Now the condition of the above written bond is such that if the sub-contractor shall duly perform and observe all the terms, provisions, conditions and stipulations of the said sub-contract on the sub-contractor's part to be performed and observed according to the true purport intent and meaning thereof or if on default by the sub-contractor the surety shall satisfy and discharge the damages sustained by the contractor thereby up to the amount of the above written bond or if a final certificate shall be issued pursuant to the provision of the main contract, then upon the date stated therein this obligation shall be null and void but otherwise shall be and remain in full force and effect ..."

On 27 March 1998 during the course of the sub-contract works, Woodbank

informed OTV that it was ceasing to trade and stopping work with immediate effect. Accordingly, OTV determined the sub-contract and gave notice to T&G of its intention to call on the bond. OTV arranged for the completion of Woodbank's sub-contract works itself and, following completion of these works, submitted substantiation of the costs incurred following Woodbank's default in an amount in excess of the value of the bond. T&G refused to honour the bond and OTV commenced proceedings. T&G raised a number of defences including:

- The final certificate issued under the main contract rendered the bond null and void.
- OTV's failure to sue Woodbank rendered the bond unenforceable.
- OTV had not proved that it had sustained all of the loss and damage giving rise to OTV's call on the bond.

Issues and findings

As a result of the wording of the bond, did the issue of the final certificate under the main contract render the bond null and void?

Not the bondsman had an obligation to discharge damages that had crystallised prior to the issue of the final certificate under the main contract.

When did the surety's obligation to discharge damages crystallise?

When a call or demand was made on the bond accompanied by sufficient evidence, particulars, supporting material or proof to enable the surety to be reasonably satisfied that there had been a default, damages incurred as a result of the default and a failure by the defaulting party to satisfy those damages.

Did the bond contain an implied condition precedent to the effect that, prior to making a call, a claim had to be made against the defaulting party?

No, such a term was neither necessary nor required by reason of business efficacy.

Had the claimant proved its loss?

Yes.

Was the claimant entitled to claim consultancy fees and administration charges as damages flowing from the failure to pay out on the bond?

Yes, the costs claimed were recoverable as damages directly and foreseeably flowing from the bondsman's breach.

Commentary

The bond here was of the nature of a guarantee and this case highlights the hurdles a party may need to overcome in order to be able to successfully call on a bond of this type. Consideration of the judgment provides helpful guidance to the approach to adopt when faced with making such a call. This case also serves as a reminder of what an unsatisfactory form of security bonds of this type can be when a bondsman takes a stand in relation to a particular bond in what was essentially a dispute about quantum.

It is worth noting the judge's willingness to allow the claimant's claim for the costs of engaging claims consultants and its internal administration costs incurred in preparing further documentation in support of the claim following the bondsman's initial rejection of the call. There seems no reason why the judge's reasoning for allowing this element of the claim should not be applied when any party is faced with a party refusing to honour an obligation to make payment.

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