AGGREGATE

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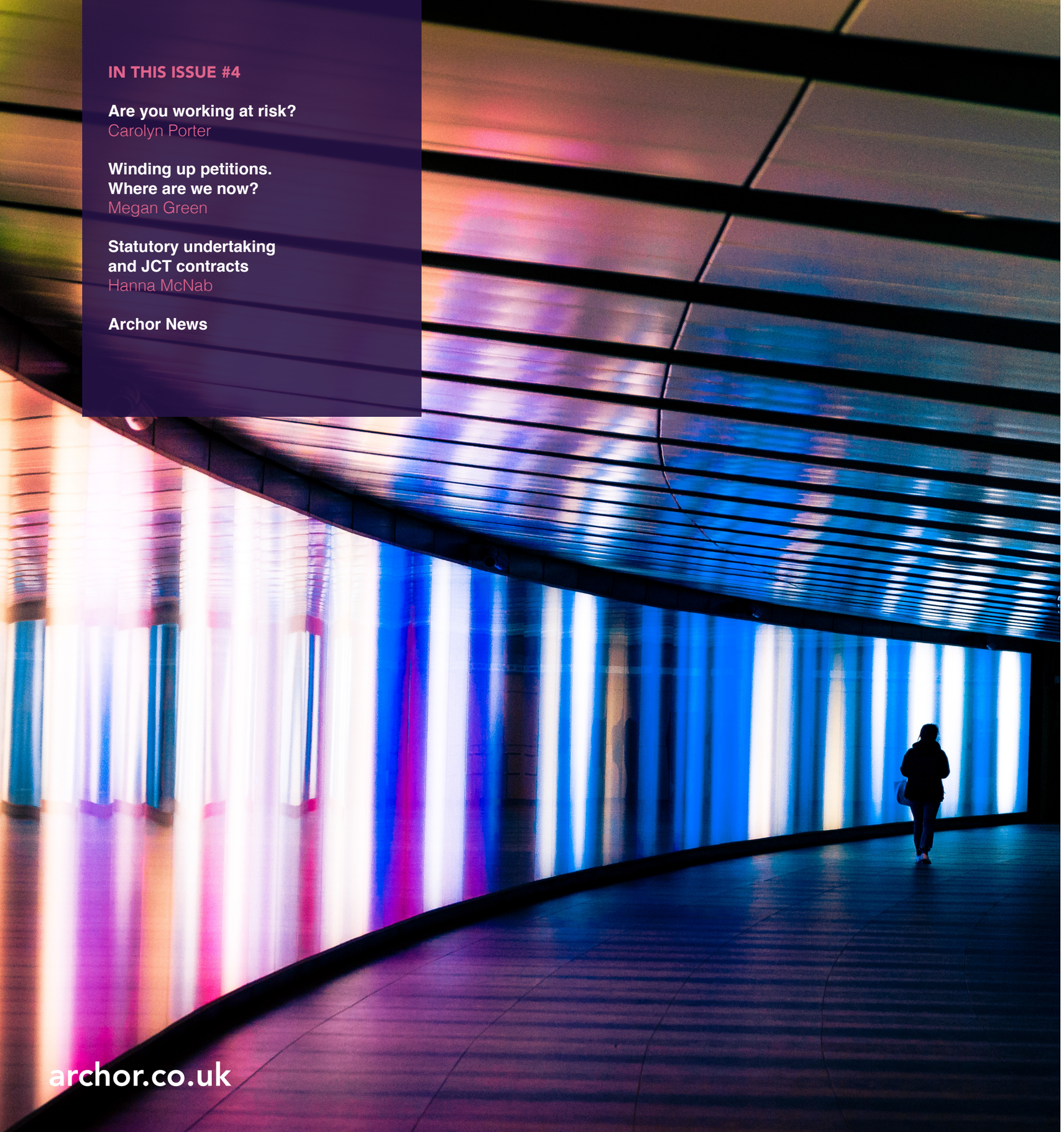

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Archor News

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Welcome to the fourth edition of Archor's Aggregate newsletter.

In this edition we wanted to look at some typical issues that come across our desks time and time again.

First, Carolyn looks at letters of intent – what are they and what are their risks and advantages? Many a dispute starts with a project involving an LOI, so knowing what's being signed up to is a must to avoid these.

Then, Hanna follows up on our recent webinar with an article on 'statutory undertakers'. A much-misunderstood area, this was one of the topics that generated the most amount of follow up questions – so Hanna has tried to consolidate the position in this article. And she's offering a prize (undisclosed!) for the first to identify the musical theme that runs through her piece.

Issues around LOIs and statutory undertakers are (nearly) as old as time, as are insolvency problems in the construction sector. We've unfortunately seen lots of recent casualties, including some big name and large turnover companies, and it's likely that trend will continue because as of 1 April, the winding up petition rules have changed again. In a nutshell, the coronavirus-related restrictions are now at an end so the threshold for issuing WUPs is back to £750 and for the first time in around two years creditors will be able to issue WUPs for undisputed debts without any other restrictions. Megan explains more in her article.

Finally, we have some news of new joiners. Most recently last month Sophie Bennett joined us, hot on the heels of Senior Associate Sarah Lester who arrived in March. Also in March Jesscia Housego became our first Trainee Solicitor , and Hayley Morgan joined us as an Associate in January. We have a brief profile on each of them. Some of you may have seen Hayley and Sarah in action in our recent webinars - the latter on collateral warranties, which remarkably given what we thought was a 'dull' subject was our best attended to date!

Happy reading – and as ever, if you have any ideas for future articles or other feedback, do please get in touch.

Oli, Editor-in-Chief

Are you working at risk?

Carolyn Porter
Partner

In the current times of grave uncertainty surrounding material prices and lead times, initially prompted in early 2020 by numerous events including covid and more recently being fuelled by the Russian invasion of Ukraine, the use of letters of intent (or LOIs) is becoming increasingly popular. However, it's important to be aware of the risks involved for both contractors and employers working under them.

What is a LOI?
A LOI is typically a letter from an employer to a contractor that expresses an intention to enter into a formal contract at a later date, and in the meantime requests that the contractor carry out certain works before the finalisation of that contract.
Why are LOIs used?

LOIs are generally used as a stop gap, to enable contractors to commence some works whilst the technical and practical elements of the full construction contract are being negotiated.

It is normally cheaper and logistically more efficient for parties to organise supply chains, procure materials, and commence site preparations as soon as possible.

LOIs can give comfort to contractors that they will be paid for preliminary works prior to entering into a full contract, while offering flexibility to employers who may not yet have finalised the full scope of the project.

In recent months the use of LOIs has become increasingly prevalent due to material price increases. Employers are desperate to get contractors to make a start on procuring materials and setting up supply chains as early as possible in an attempt to fix prices for certain elements of the works at an early stage.

Are LOIs binding?
Whether or not a LOI is binding is a matter of interpretation and every case will turn on its facts. Courts will look at whether parties intended to create legal relations. It is therefore important when seeking to create a binding LOI to ensure that the LOI is signed by both parties, provides for consideration (i.e. payment in return for services carried out) and sets out a clear arrangement as to the ultimate aim of the LOI.

The general principle is that provided there is agreement over the essential terms and that it is acted out by the performance of the parties, the LOI will be a binding contract. Conversely a lack of agreement over terms essential to the operation of a basic interim contract will normally be fatal to the characterisation of a LOI as a binding agreement.
What if the LOI isn't binding?

Where a LOI is found to be non-binding but work has still been started, there will often be uncertainty around some fundamental matters, such as time to complete the works, site access, control over materials and relationships with third parties, which is likely to lead to disputes.

A non-binding LOI is not always bad news though. While it will ordinarily be preferable to have a clear and binding LOI for both parties to rely on, a non-binding LOI does not leave the contractor with no rights. Often works carried out under a non-binding LOI will be payable on a 'quantum meruit' basis, so that contractors are paid a reasonable sum for the works completed. And counterintuitively, in certain circumstances that is the best position to be in...

Watch out for the cap
It has long been the case that if there is a cap within a LOI (be that financial, scope of time related) and the contractor exceeds that cap, they will be legally exposed. This is important: often contractors believe they will be paid a reasonable sum for any works undertaken over and above the cap, but that is not the case.

There are two main exceptions to this rule. First, contractors will be entitled to payment on a quantum meruit basis if no binding contractual relationship ever existed (as mentioned above).
Second, contractors may be entitled to payment on a quantum meruit basis over the cap if it is held that the parties have impliedly agreed a variation to the LOI so as to increase the cap, without actually entering into a formal contract. However, this is notoriously hard to prove and so it is always recommended that contractors agree to increase the cap before reaching the limit, or in the absence of such agreement that works cease (or at least pause) once the cap is reached.

How does an LOI end?
In an ideal world, a LOI will come to an end once a formal contract is entered into. It is preferable for LOIs to expressly set out that any contract (once executed) will supersede the terms of the LOI, and also that the contract will apply retrospectively to all works carried out under the LOI.

However it is not unheard of for LOIs to run for the entirety of projects, with the parties never agreeing a formal contract and consistently increasing any caps (or LOIs being uncapped in the first place).
Further, especially in the current market, there will be situations where one or both parties may not wish to enter into a formal contract. Whilst LOIs will not place an obligation on either party to enter into a formal contract, often LOIs do not clearly deal with termination of the LOI itself. It is therefore also advisable to include provisions which enable either party to terminate the LOI in certain pre-agreed circumstances.

If a LOI sets out an expiry date, the same principle applies as with a cap: contractors should stop works on that date unless an extension to the LOI is agreed in writing.

If the parties continue to carry out works following the expiry of a LOI but before a contract is finalised the legal position can be very difficult to predict. The Courts may hold that no contract exists, that the terms of the (not yet executed) contract apply, or that different terms entirely apply. This difficulty was demonstrated in RTS Flexible Systems v. Molkerei [2010] where the Court at first instance, the Court of Appeal and then the Supreme Court all reached three completely different decisions on what the applicable contract terms were.

The moral of the story?
Lord Clarke of the Supreme Court put it quite well in that Molkerei case: "the different decisions in the courts below and the arguments in this court demonstrate the perils of beginning work without agreeing the precise basis upon which it is to be done. The moral of the story to is to agree first and to start work later".

Winding up petitions Where are we now?

Since June 2020, we have seen a temporary halt of issuing winding up petitions (WUPs) without certain conditions being met.

Most recently, those coronavirus-related restrictions meant that a creditor could issue a WUP for an undisputed debt above the increased threshold of £10,000 (normally £750) provided that the additional conditions set out in Schedule 10 to the Corporate Insolvency and Governance Act 2020 were met. These were:

- A creditor could not present a winding-up petition in respect of excluded debt, which was defined as debt in respect of any sum payable by a tenant under a business tenancy that is unpaid by reason of a financial effect of coronavirus.

- A creditor could not present a winding-up petition unless written notice (a Schedule 10 Notice) had been delivered to the debtor confirming that the requirements of Schedule 10 have been met, and either that no proposals for payment of the debt were made or a summary of the reasons why the proposals made were not to the creditor's satisfaction.

However, these rules stopped applying from 31 March 2022.

The new rules

Commercial landlords are no longer prevented from issuing a WUP in respect of unpaid rent which has accrued due to the economic effect of the coronavirus pandemic. So, commercial tenants will no longer be protected from eviction. However, the Government have proposed to implement a rent arbitration scheme to deal with commercial debts which accumulated during the coronavirus pandemic.

Creditors who are owed less than £10,000 are once again able to present WUPs – the old threshold of £750 is back. This means that debtors who owe sums less than £10,000 can once again be on the receiving end of WUPs – and so need to be on the lookout for them, and making sure that all debts are settled on time (or arrangements reached if for any reason they can't be).

Debtors previously had the opportunity to make proposals for payment (albeit not necessarily actual payment!) and introduce prospects of resolving the debt within 21 days of receiving notice before a WUP could be formally presented. However, the rules are now reverting to pre-coronavirus times where it is not required to give notice of a WUP – so debtors could receive one at any time!

Beware of the WUP

It is expected that WUPs will become more prevalent now the Schedule 10 Conditions have been lifted. For the first time in around 2 years, creditors are able to issue WUPs for undisputed debts without any restrictions other than the relatively modest £750 threshold.

If you're owed money they can be a very useful means of recovery. But if you're a debtor, as we've discussed previously, you must act quickly if you are presented with a WUP, not only due to the detrimental effect it can have on the day to day running of your business, but also due to the risk of other creditors joining the WUP, increasing the creditors you must pay.

The removal of the remaining restrictions will be a shock to the system. So, if you are on either side of the fence, requiring advice in connection with the issue or defence of a WUP, get in touch.

Megan Green
Paralegal

Statutory undertaking & JCT contracts

If you're a Dedicated Follower of Archor, you'll know that we recently hosted a webinar where we discussed the construction law questions everyone's too afraid to ask. One of the topics I dealt with during the webinar was a contractor's entitlement to an extension of time due to delays caused by statutory undertakers. Perhaps unsurprisingly, I've had a few questions e-mailed to me about this subject following the webinar, so I thought I'd set out the position in an article (with a prize for whoever emails me first with the hidden song theme running throughout!).

One of the most common causes of delay on construction projects is a delay caused by statutory undertakers. Given how frequently this arises, it is important for all parties to understand whether the contractor is entitled to an extension of time because of such delay under the contract.

For the purpose of this article, I am going to focus on the wording in a JCT Design & Build Contract 2016, which provides that one of the Relevant Events is "the carrying out by a Statutory Undertaker of work in pursuance of its statutory obligations in relation to the Works, or the failure to carry out such work" (clause 2.26.7) and apply the relevant case law to such wording.

The first significant case

The first case to consider is Henry Boot Construction Ltd v. Central Lancashire New Town Development Corp [1981]. Henry Boot was the contractor, constructing a housing estate for Central Lancashire. Henry Boot, Tired of Waiting for statutory undertakers to carry out their works, claimed an extension of time for the associated delays. The actual detail on the case is scant, but Judge Edgar Fay QC's judgment is clear. He held that where a statutory undertaker was carrying out work pursuant to a contract it was not covered by clause 2.26.7 (or similar). This is because the work being carried out by the statutory undertaker was not in pursuance of its statutory obligations, but rather under a contract.

Taking a short example: one Sunny Afternoon, a sewer on a construction site becomes blocked. A Waterloo Sunset passes and Anglian Water enters the site, using its statutory powers to do so. Anglian Water proceeds to carry out the necessary works to unblock the sewer: this takes All Day and All of the Night. In doing this, Anglian Water causes a delay to the contractor's works. In this scenario, the contractor is entitled to an extension of time under clause 2.26.7 as the delay has been caused by Anglian Water carrying out works "in pursuance of its statutory obligations" (assuming the blockage has not been caused by the contractor itself). However, in practice, this rarely occurs.

The far more common scenario concerning statutory undertakers is where works are carried out under a contract, either with the employer or the contractor. In this scenario, the statutory undertaker is not carrying out works under its statutory obligations, but rather under a contract. If this is the case, then there is no entitlement to an extension of time under clause 2.26.7.

The contractor may be entitled to an extension of time under a different Relevant Event if the contract was entered into between the employer and the statutory undertaker, however if the contract is with the contractor then any delay by the statutory undertaker is the contractor's risk.

Considering the Henry Boot test

More recently, in Jerram Falkus Construction Limited v. Fenice Investments Inc [2011], the TCC suggested that the test in Henry Boot may need to be revisited following the extensive privatisation of the utilities industries that has occurred since 1980. However, it noted that if a party is performing a function that is equivalent to a statutory undertaker then that party should be categorised as a statutory undertaker. As such, Henry Boot remains good law.

Application of clause 2.26.7 in practice

In practice, it is rare for statutory undertakers to be carrying out works in pursuance of their statutory obligations. Typically, it is the contractor who enters into a contract with the statutory undertaker for specific works relating to the project. If the statutory undertaker's works are late in this instance, then the contractor takes the risk for any delay and is not entitled to an extension of time under clause 2.26.7.

There are in fact very few circumstances when clause 2.26.7 will actually bite, as a contract will usually be in place with the statutory undertaker. It will therefore be necessary to look at who has entered into this contract: the employer or the contractor. However, regardless of the contracting party, the contractor cannot rely on clause 2.26.7 for an extension of time.

You Really Got Me?

I expect by This Time Tomorrow, having read this article, there may be some difficult conversations taking place about a contractor's entitlement to an extension of time by virtue of clause 2.26.7.

Hanna McNab
Partner

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ARCHOR NEWS

We're delighted to announce some new joiners to Team Archor.

Most recently, Sophie Bennett has joined us as a paralegal. Sophie has experience of paralegal work in the construction team of an international law firm so she will be a real boost to our already excellent paralegal team.

In March, Sarah Lester arrived as our first Senior Associate. Sarah has a wealth of experience in the construction sector having worked at a large main contractor for around 15 years before joining the dark side of private practice. She specialises in non-contentious construction law where from her previous in-house role she has experience of advising on risk management, insurances, bonds, PCGs, sub-contracts and main contract negotiation, as well as advising on contentious matters and assisting with claims and adjudications.

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Shortly before Sarah, Jessica Housego joined us as our first Trainee Solicitor at the start of March. Jessica previously worked with the Archor partners as a paralegal so she already has plenty of experience of construction law (and of the partners' various demanding needs!). And our first new joiner of 2022 was Hayley Morgan. Hayley joined us from a local authority, where she gained experience of disputes and development work. Before that she worked at a well-known construction consultancy where she was involved with project support and documentation, becoming familiar with construction standard forms and procurement structures. She also undertook a Master's degree in Alternative Dispute Resolution, and is a qualified mediator with the Society of Mediators.

We are very pleased, and very lucky, to be able to welcome all three to Team Archor and excited to see their careers develop with us. The firm is considerably stronger for having them, and we hope you as clients and contacts will enjoy working with them as much as we do.

Attendees at our recent webinars will already have had the chance to see Hayley and Sarah in action. In March, Hayley was joined by Ruth and Hanna addressing some common construction law questions. Then in April, Sarah was in front of the camera along with our very own Mr Dull (Andrew!) discussing, by popular demand (believe it or not), the very dull topic of collateral warranties. Or at least we thought it was dull – but it was our best attended webinar to date, so what do we know…?! Ideas for our next webinar are always welcomed.

Three of our recent joiners: (L-R) Hayley Morgan, Sarah Lester, and Jessica Housego.

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