AGGREGATE

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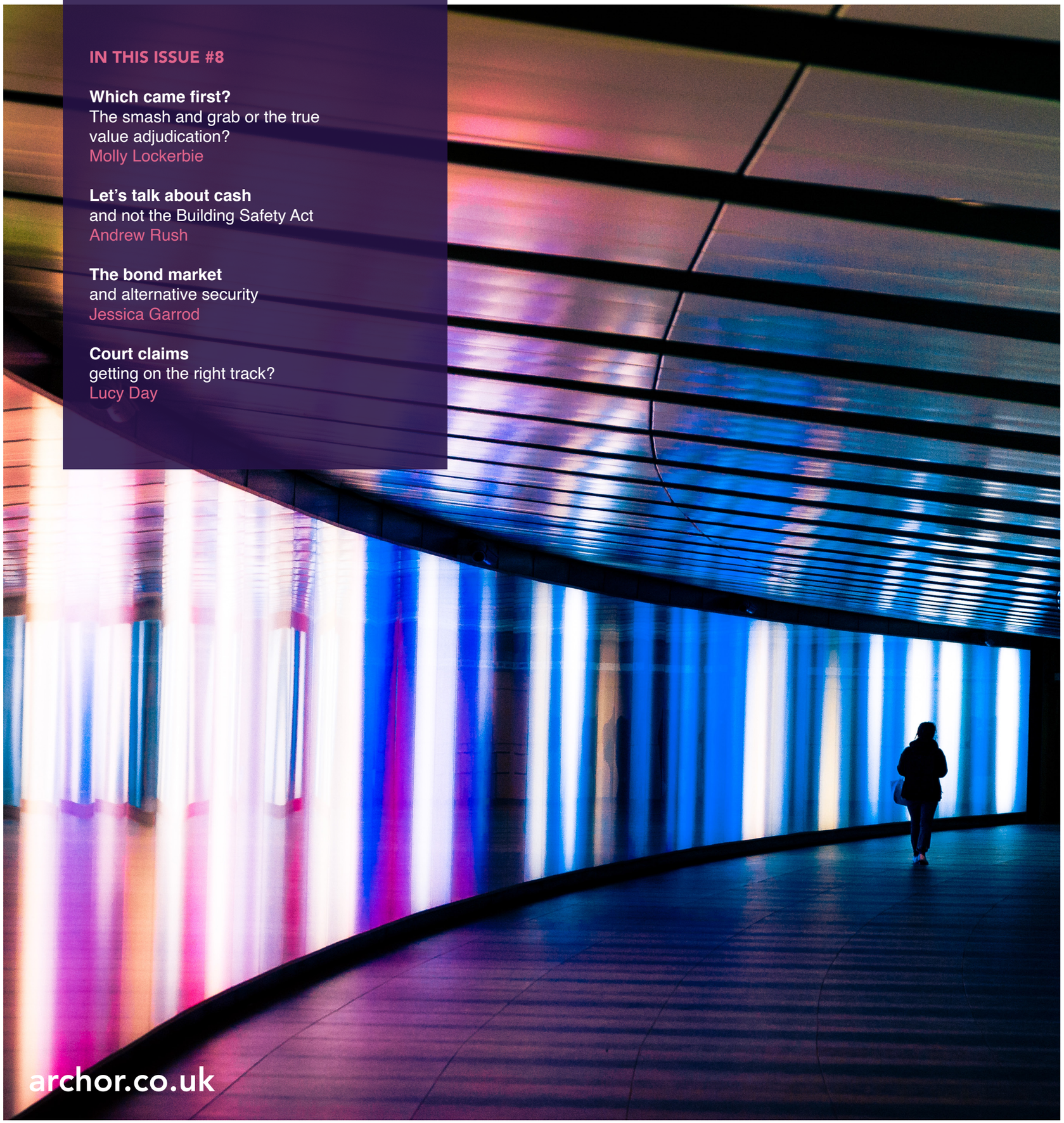

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Welcome to the latest edition of **Archor's Aggregate** newsletter.

We're into the busy period in the run up to (say it quietly) Christmas – schools are back, nights are closing in, and everyone is focusing on hitting their year end targets. Hopefully this edition of Aggregate offers a little break from the norm.

In this edition we have four articles for your enjoyment:

- Molly considers a recent case that looked at a question that has been floated since the decision in Grove v. S&T five years ago – can a true value adjudication be commenced before a smash and grab? The court's answer perhaps leaves further room for uncertainty.

- Andrew was asked to write about the Building Safety Act, but as a man who likes to play by his own rules, his article takes a different turn...

- Jessica – neatly following on from Andrew's (as it turned out) – looks at alternative security options given much publicised difficulty in the construction bond market.

- And finally Lucy looks at a new 'track' in the court system designed to make costs recovery more certain for mid-tier claims. Whether this is an alternative to or boon for adjudication remains to be seen.

We hope you enjoy this edition, and as ever, if you have any ideas for future articles or other feedback, do please get in touch.

Oli, Editor-in-Chief

WHICH CAME FIRST?

THE SMASH AND GRAB, OR THE TRUE VALUE ADJUDICATION?

Molly Lockerbie
Trainee Solicitor

If you're an avid construction law fan, or really just someone involved in construction, you'll know that the 'smash and grab' is one of the most common types of adjudication.

A smash and grab is one in which, where there is the absence of a valid and timely payment notice and/or pay less notice, the payee claims payment of the entire sum claimed in the relevant payment application. In these kinds of adjudications, the adjudicator isn't invited to decide whether the sums applied for within the payee's application are accurate, just whether or not the paying party has issued a valid notice in response. If they haven't, it's a 'smash and grab' win for the unpaid party.

On the other hand, a 'true value' adjudication is one in which the adjudicator does have jurisdiction to undertake a valuation of the relevant application for payment. The adjudicator will establish the true value of the relevant application and payment notice and as such, whether or the sum claimed by the payee is accurate. If the payee has been underpaid they will usually be entitled to the difference.

Timing of the essence?
A true value adjudication frequently follows the decision made in a smash and grab – a payee will go after the latter because it is quicker and cheaper, but faced with a loss on a technicality, the payer will often want to redress the balance by determining the true value of the interim payment.

The Court of Appeal's judgment in S&T (UK) Limited v. Grove Developments Limited [2018] held that a paying party is permitted to adjudicate on the true value of a payee's interim application, despite the fact that a payment notice or pay less notice was not given and the payee has been awarded the sum claimed in a smash and grab adjudication, so long as the payment was made. This all seems reasonable, giving an employer a chance to disprove a sum if there is no merit behind it. However, the waters have since been muddied in circumstances where a party issues a true value adjudication whilst a smash and grab adjudication is ongoing…

A new consideration
In the recent case of Henry Construction Projects Ltd v. Alu-Fix (UK) Ltd [2023], the Court held that a true value adjudication could not be started while a smash and grab adjudication was ongoing, despite the fact that the earlier awards had been paid.

Alu-Fix commenced a smash and grab adjudication claiming that sums were due to have been paid on or before 13 December 2022, which Henry disputed on a genuine basis maintaining that it had issued valid pay less notices. In the meantime it had started its own true value adjudication (with another adjudicator) as a protective measure claiming that it has previously overpaid by c.£235k, but notably this was after 13 December 2022.

The smash and grab decision found in favour of Alu-Fix, finding that the pay less notices were not valid and therefore the sum claimed should have been paid by the final date for payment of 13 December 2022. Upon receiving this decision, the true value adjudication was stayed until Henry made payment of the smash and grab award, which it did, and the true value adjudication continued.

The true value adjudicator subsequently found in favour of Henry. However, Alu-Fix disputed that the second adjudicator had jurisdiction since the true value adjudication was commenced prior to payment of the smash and grab award, and therefore refused to pay. As such, Henry launched enforcement proceedings against Alu-Fix, arguing that it had made payment of the smash and grab award and that at such time it launched the true value adjudication, there was a 'genuine dispute' in regard to the validity of the pay less notices.

The Court's decision
The Court applied the principles of Grove, specifically that a party could not commence a true-value adjudication until it had discharged its immediate payment obligation. The key issue here was that although Henry had made payment following the adjudicator's decision, the payment had not been made when the immediate payment obligation arose.

Henry maintained that while the smash and grab adjudication was ongoing, there was a genuine dispute as to whether there was an immediate payment obligation, so therefore there should be no limitation as to when the true value adjudication could have commenced.

The Court found that the final date for payment of the smash and grab fell on 13 December 2022, and therefore the immediate payment obligation was not discharged at the time that Henry commenced the true value adjudication. The argument put forward by Henry that there was a 'genuine dispute' at the time the true value adjudication was commenced was considered by the Court but it said this posed a risk of influencing the right of the payee to be paid. Therefore, it was found that the second adjudicator did not have jurisdiction and Alu-Fix were not required to pay the sum awarded to Henry.

It was added by the Court that had the smash and grab decision been such that the pay less notice issued by Henry was valid, it would have removed the immediate payment obligation. In such circumstances, the true value adjudication decision would have been enforceable.

Comments
This is one of the points that has been debated since the decision in Grove and effectively indicates that a true value adjudication cannot be commenced while there is uncertainty about a smash and grab. For the time being, if a smash and grab adjudication is commenced it will probably mean that a true value adjudication cannot be commenced even if the smash and grab is disputed on genuine grounds, because an adjudicator asked to consider the true value adjudication will likely decide they have no jurisdiction until the smash and grab is resolved.

Although the court suggested that jurisdiction would have been in place for the true value adjudicator in this case if the smash and grab had been resolved in Henry's favour, this effectively introduces a type of contingent jurisdiction which adds considerable uncertainty to all parties. It remains to be seen whether a higher court would agree with the court's analysis in this case, and we think it is likely that at some point the question is likely to arise again. For example, could a party faced with a true value adjudication raise a deliberately unmeritorious smash and grab adjudication as a time-buying tactic?

Normally we say that the way to resolve these issues is to make sure that any payment or pay less notice is validly issued to avoid the dispute in the first place – although whether that's the case if completely unmeritorious smash and grabs are allowed to frustrate a true value adjudication remains to be seen…

LET'S TALK ABOUT CASH (and not the Building Safety Act)

I was tasked with writing an article on the Building Safety Act ("BSA"). Now for those involved in Higher Risk Buildings, this is of course vitally important to understand, but in truth it does not impact on 95% of the construction industry. Lawyers love to write about law stuff and you will find lots of great articles on the BSA, but most of our clients are more focussed on getting paid for what they have done.

We work for clients with turnovers ranging from £½million to £4 billion and they all have the same issue – getting paid.

So I'm going to let others talk about the BSA this time, and focus on some simple options for getting paid.

Option No. 1 - Your right to suspend

If you are working on a job and not getting paid, the most powerful tool is often exercising your right to suspend your works. Every party has a statutory right to suspend on the giving of 7 days' notice if they have not been paid sums due under their contract.

There needs to be an element of caution, as sums have to be due, so if you have a nil payment notice / pay less notice that has been validly issued, this right is not open to you, even if you know you are in practice owed money. However, assuming there is a clear sum owing, the ability to suspend is a very powerful tool.

Why would you not use this if you are owed money? You'd be mad to keep working and keep spending you own money, wouldn't you? I say this slightly tongue in cheek as we are all reluctant to take such action, but any rational person would say 'I will do no more until I am paid'. All too often we see a scaffolding company, or a plastering company (for example) owed tens, if not hundreds of thousands of pounds by a main contractor who has gone into insolvency and we all wonder how they got into that situation. They no doubt listened to false promises and kept working.

Option No. 2 – Adjudication

For those of you who are experienced in going through adjudication, you will know that it is 'rough and ready'. And yes, it's not perfect. And yes, sometimes you wonder what the Adjudicator was thinking (although occasionally this benefits you!). But it is quick and efficient and does work to get money moving.

Also, for those debts below £100k there are a number of possibilities to keep adjudicator's fees down. One such example is the Construction Industry Council Low Value Disputes process, which does not need the parties' agreement. So if your contract is ad hoc (let's say for example a PO, an email exchange etc) you can use this process.

We find ourselves still bringing a lot of adjudications over sums where no valid payment / pay less notice has been issued – 'smash and grab' adjudications. These are quick to do, not costly, and have a high success rate for fairly obvious reasons. Another myth is lawyers' fees are more expensive than commercial consultants' fees – not all lawyers (or at least, not ours…).

Option No. 3 - Winding Up Petitions (WUP)

During Covid times, there was a hiatus on winding up petitions, but the position is now back to normal. So, if you are owed money and there is no dispute about this – where it's a case of can't or won't pay rather than a genuine dispute – the use of a WUP should be considered.

The real issue with WUPs is the fact that once one is issued, everyone piles in and for the company against whom the petition is issued, they have to fight off a whole host of creditors before they can get the WUP withdrawn – so the threat of issuing one is often enough to get paid. WUPs are not to be used lightly and need to be carefully considered, but if the sum is owed and no cross claim or dispute has been raised they can be a good option. Also you do not need to issue a statutory demand if you are bringing a WUP against a company – this only applies against individuals.

Conclusion

Most of you will know the above and I know that it is easy to talk about these things rather than do them. There is always a commercial angle to this, but ask the creditors owed millions from any of, to name but a few, Buckingham Group, Henry Construction, Claritas Group and Tolent Construction, if they wish they had got onto the sums owed quicker. I think you know what the answer will be.

The market is tough. When I speak to clients those in the civils sector are finding it easier than those in the building sector, but no one is finding getting paid simple – whatever tier or level in the chain you are.

So we all know cash is the lifeblood of the construction industry – cash is king. As I often say to clients, trust the process. And use the time you've saved by getting payment in early to find a good article on the BSA…

Andrew Rush
Senior Partner

THE BOND MARKET AND ALTERNATIVE SECURITY

There has been a record-breaking number of construction insolvencies in the UK over the past twelve months - in March 2023 alone, 38 construction companies entered into administration. In the last two months we have seen two high profile insolvencies: Henry Construction and Buckingham Group (two large contractors turning over £402m and £665m respectively), have entered into administration.

But will these insolvencies have a detrimental effect on the bond market? The answer is yes – these insolvencies are large insured exposures for the surety market and, as a result, it has taken a blow. Bond providers are now seeking to manage risk by tightening bond capacity. Brokers and bond providers are warning contractors that it will now be significantly more difficult to obtain bonds in light of the high-profile insolvencies we have seen this year and, further, if contractors are able to obtain bonds, it is likely they will be paying a hefty premium.

Surety in the construction industry is an important tool to provide protection to all parties involved in a construction project. But if providers are tightening bond capacity, and contractors cannot procure bonds, how else can parties get this protection? We have considered three alternative forms of security commonly used in construction projects.

Parent Company Guarantee

A parent company guarantee (PCG) is granted by the parent (or holding) company of a party to guarantee the performance of the subsidiary company's contractual obligations.

A true PCG can only ever be a secondary obligation (and not a primary obligation). The significance of this is that a true PCG can only be triggered in the event the contracting party defaults on its obligations under the contract. However, parent companies should ensure the document that outlines the PCG clearly states the parent is only liable in the event of a default by the subsidiary company. Otherwise, the PCG may actually be an indemnity and confer a primary obligation on the parent company – a far greater undertaking because an indemnity is independent of the underlying contract and will be valid even if the underlying transaction is set aside – a guarantee will not.

Further, in order for a true PCG to be enforceable it must be in writing (and if you are as boring as I am then you will know this is a requirement of section 4 of the Statute of Frauds Act 1677). However, unlike guarantees, indemnities can be made verbally.

Most commonly, PCG's are granted in favour of the developer of a construction project to guarantee the performance of the main contractor, although in theory they can be offered by any parent or linked company and in respect of any contract (e.g. a contractor could require a PCG from a key sub-contractor). It is important to make sure that the company giving security is itself of good standing though, otherwise the security may end up being worthless.

Escrow Agreements

The purpose of an escrow is usually to provide a fund which the contractor can draw in the event of the employer defaulting on payment. Often, in construction projects, escrows are used when the employer's solvency is not certain (such as when the employer is a special purpose vehicle incorporated specifically for the project in question). However, recently we have seen a number of escrows used in a different way. For example, we acted for a main contractor who was required to enter into an escrow agreement as it was unable to obtain a bond.

The way escrows work is simple - a pot of money is paid into an interest-bearing bank account. The escrow account that holds the money is held by an escrow agent, typically a solicitor or someone appointed by the solicitor.

The escrow sum will be paid out of the account in the event of certain triggers. The terms of the escrow are recorded in an escrow agreement – most of the time, these terms will require the escrow sum to be topped up if paid out.

Direct Payment Arrangements

Direct payment arrangements in a construction project involve money moving directly from one party to another and bypassing the party in the middle. For example, the employer paying the sub-contractor directly and bypassing the main contractor.

Direct payments are used when the middleman (in this scenario, the main contractor) has limited financial stability. They protect the employer in the event that the contractor becomes insolvent by ensuring that funds paid are actually used in respect of the project rather than diverted to other projects. However, it is very important if any direct payment arrangements are to be to put in place that there is clear unambiguous wording in writing, otherwise disputes may arise and the employer may end up paying twice for the same work.

Conclusion

There are plenty of alternatives to bonds which are worth exploring now the market has become more difficult. The most important thing though is for the parties to consider what security they actually need and whether it is worth the price that is demanded – different forms of security come with different costs and difference risks.

The time to consider these things is prior to entering into a contract, because afterwards if there is no security required there will be no ability to demand it; and conversely, if a form of security has been offered that cannot be delivered (such as a bond) then the promising party may have a problem.

Jessica Garrod
Trainee Solicitor

COURT CLAIMS

GETTING ON THE RIGHT TRACK

For decades, the English legal system has operated on the basis that the losing party generally pays the winning party's legal costs, but the question of how much of those costs will be recovered by the winning party always remains uncertain. For commercial claims with a value up to £100,000, this is about to become a whole lot clearer – in theory at least – with the introduction of a new Intermediate Track and the extension of the Fixed Recoverable Costs (FRC) regime.

As of 1 October 2023, the FRC regime will be extended to cover all in-scope Fast Track and Intermediate Track claims up to £100,000. There will be no limits imposed on the amount legal representatives can charge, but the FRC regime aims to provide clarity and predictability as to costs that are recoverable from the unsuccessful party. The changes to the FRC regime and the new Intermediate Track will be introduced by CPR 45.

New Intermediate Track

The existing 'Tracks' to which the court allocates claims will remain, with the addition of a new 'Intermediate' Track:

- Claims with a value under £10,000 will usually be allocated to the Small Claims Track (sometimes referred to as the 'Small Claims Court');
- Claims with a value between £10,000 and £25,000 will usually be allocated to the Fast Track;
- Claims with a value between £25,000 and £100,000 will usually be allocated to the Intermediate Track; and
- Claims with a value over £100,000 will usually be allocated to the Multi-Track (where the FRC regime does not apply).

Judges will continue to hold discretion to allocate a particularly complex claim that has a value under £100,000 to the Multi-Track. A non-monetary claim will not be allocated to the Intermediate Track unless the court decides otherwise.

The idea of the Intermediate Track is to make claims of these values more efficient. Statements of case will be limited to 10 pages, witness statements will be limited to 30 pages, and only one expert witness will be permitted per party (unless the court directs otherwise). Expert reports are to be limited to 20 pages (excluding photographs) and oral evidence will be time limited.

Banding and Costs

The complexity of cases that fall within the Fast Track and Intermediate Track will be assessed and assigned to a 'band', which determines the level of costs that are recoverable. Both Tracks will have four bands, and the higher the band, the higher the level of recoverable costs. It is for the court to decide which band within a Track the claim should be allocated to.

Band 1 of the Intermediate Track will cover more simple claims with only one issue in dispute, where the trial is not expected to last more than one day. Band 2 will cover claims where there is more than one issue in dispute, including liability and quantum disputes. Band 3 of the Intermediate Track will cover cases that are more complex than Band 2, with Band 4 covering cases that are the most complex, where the trial is not expected to last more than three days.

Tables of fixed costs have been released within PD 45 (draft for early publication) detailing the amount of costs recoverable at each stage according to the Track and band of complexity of a claim. The FRC regime will also provide for recoverable pre-action costs.

Conclusion

Construction claims below £100,000 are typically difficult to pursue because of high legal costs and a lack of certainty about costs recovery. The threshold effectively moving from £25,000 to 100,000 therefore represents a considerable move forward, with lots of claims being taken out of the most complex track.

However, until the system has bedded in, it's unlikely that construction parties will be ditching tried and tested adjudication in favour of court proceedings for claims below £100,000, even though the prospect of costs recovery is an attractive counterbalance to the speed of adjudication. We do not yet know how banding will work, and the courts remain generally overworked meaning it can take a long time to get a decision.

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