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

Dispatch

Case Update: omission of works NEC3

Van Oord UK Ltd v Dragados UK Ltd

[2021] ScotsCS CSIH_50

We discussed this case in Issue 244. In short, in the course of 2018 and 2019, Dragados issued various Contractor's Instructions to omit certain areas of soft dredging from Van Oord's works. This work was transferred to the other subcontractors. Dragados further said it proposed to reduce the sum payable for Van Oord's remaining work under the "compensation event" provisions of NEC 3. The reduction ranged from £7.48 per cubic metre to £5.82m then £3.80m. Van Oord contested the reduction on the basis it was invalid, as Dragados had breached the subcontract. It sought payment at the original bill rate.

The Judge, at first instance, said that, in terms of the NEC3 contract here, the omission of work did constitute a breach of contract. And the contract then went on to specify the remedy – and, indeed, the only remedy – available for a breach of contract, namely that it was a compensation event. Further, Dragados was entitled to reduce the bill rate payable to Van Oord for the remaining works. The Judge said that he had reached this conclusion without having to place any significant weight upon clause 10.1:

"The Contractor and the Subcontractor shall act as stated in this subcontract and in a spirit of mutual trust and co-operation."

Van Oord appealed to the Inner House on the question of whether or not Dragados was entitled to reduce the sums payable to Van Oord? Lord Woolman noted that the theme of unfairness underpinned Van Oord's position. Van Oord said that Dragados was seeking to manipulate the contract in its favour. Had Van Oord known that it would be left with a disproportionately higher share of the more difficult work, it would have increased the dredging bill rate in its tender. Dragados said that NEC3 provided a "blueprint" for the circumstances that had arisen and that the recalculation yielded a fair result to Van Oord, which would otherwise receive a windfall benefit.

The Judge noted that the NEC3 consisted of a series of interlocking terms, including Clause 10.1. In the view of Lord Woolman, Clause 10.1 provided a useful starting point. It was not: "*merely an avowal of aspiration.*" It reflected and reinforced the general principle of good faith in contract. It also aligned with a number of key propositions of contractual interpretation:

(i) A contracting party "*will not in normal circumstances be entitled to take advantage of his own breach as against the other party*": *Alghussein Establishment v Eton College;*
(ii) A subcontractor is not obliged to obey an instruction issued in breach of contract: *Thorn v The Mayor and Commonalty of London* (1876);
(iii) Clear language is required to place one contracting party completely at the mercy of the other: *Parkinson (Sir Lindsay) & Co. Ltd v Commissioners of His Majesty's Works and Public Buildings* [1949].

The court concluded that: "*Unless Dragados fulfils its duty to act 'in a spirit of mutual trust and co-operation', it cannot seek a reduction in the prices.*"

Did Dragados act in a spirit of mutual trust and co-operation? In short, no. Each breach by Dragados constituted a compensation event. Although NEC3 contains a complex formula to assess the value of a compensation event, that was not needed as the Parties agreed there was a reduction in the Defined Cost. They disagreed on whether there was also a reduction in the prices and the bill rate payable for the remaining work.

The court concluded that, properly construed, clause 63.10 applied only to a lawful change. It excluded instructions issued in breach of contract. They were invalid, because they were not given "in accordance with this subcontract". The natural synonym for "in accordance with" is "consistent with". A breach was plainly inconsistent with the contract. The court further added that this meant that all breaches were treated equally. Second, it avoided the suggestion that Van Oord was bound to obey a "breach instruction". That could not be right. Third, and finally, the NEC3 should not be a charter for contract breaking.

Case Update: adjudication & insolvency

John Doyle Construction Ltd v Erith Contractors Ltd

[2021] EWCA Civ 1452

We reported on this case in Issue 244. JDC (who were in liquidation) sought to enforce an adjudicator's decision. At first instance, the TCC held that the security available (or which was said to be potentially available, were the judgment sum to be paid over) was insufficient and the summary enforcement application was refused. On appeal, JDC said that there were alternative offers of security which the Judge did not address in his judgment. For example, JDC said that the TCC should have found that not only that the liquidators had themselves offered security, but that the security which they had offered, being the payment of the judgment sum by Erith into an escrow account or into court, was adequate. This potential "offer" was not addressed by the Judge. JDC further said that a Deed of Indemnity would be engaged if proceedings were commenced by Erith. Erith said that did not constitute an offer of security at all.

However, Coulson LJ also identified that "*lurking in the shadows*" of the appeal was a wider point, as to whether a company in liquidation, with an adjudication decision on its final account claim in its favour, but facing a continuing set-off and counterclaim, was entitled to summary judgment at all. In *Bresco* (Issue 241), the Supreme Court had made it clear that a

company in liquidation was entitled to commence and pursue an adjudication, and that to do so was not a futile exercise. But here, JDC suggested that the Supreme Court went further and decided that a company in liquidation was entitled to summary enforcement of a decision, regardless of the absence of a final determination of the other side's set-off and cross-claim.

As a starting point, given that it has been 25 years since the introduction of the adjudication legislation. Coulson LJ noted:

"In reality, it is the only system of compulsory dispute resolution of which I am aware which requires a decision by a specialist professional within 28 days, backed up by a specialist court enforcement scheme which (subject to jurisdiction and natural justice issues only) provides a judgment within weeks thereafter. It is not an alternative to anything; for most construction disputes, it is the only game in town."

The Judge added that a claimant company in liquidation, seeking summarily to enforce an adjudicator's decision, should take all necessary steps to ensure at the hearing that it is clear to everyone what issues need to be decided. However, he added that *Bresco* noted the potentially complex issues that can arise between the parties where the claimant is in liquidation. Such a burden should not be underestimated. In particular:

"Any undertakings or security being offered by a claimant company in liquidation need to be clear, evidenced and unequivocal. It is not for the judge to point out during the hearing potential inadequacies with the security offered, in order to give the claimant an opportunity to amend its offer on the hoof in the hope of making it more acceptable. Neither is it for the judge to endeavour to turn vague suggestions by counsel, in the cut and thrust of oral argument, into a potentially binding agreement between the parties...Such an approach gives rise to confusion and potential injustice. If a claimant wants to summarily enforce the adjudicator's decision, notwithstanding its own liquidation, it needs to be unequivocal about any offer that it is making to ring-fence that money or otherwise protect it. Where there is a dispute about the sufficiency of the undertakings or security on offer, it must at least be beyond argument what has been offered and why."

Here, Coulson LJ noted that the way in which JDC approached the case meant that it was not always clear, either to Erith or the Judge, what it was that JDC were actually offering, or on what basis. There was never any clear offer by JDC's liquidators of a simple and straightforward undertaking to provide sufficient ring-fencing of the money in issue. This gave rise to inappropriate levels of complexity and confusion. The question for the CA was, did the liquidators of JDC make a clear and unequivocal offer that Erith should pay the sum identified in the decision into an escrow account or into court, which would then serve as the necessary security for Erith's set-off and counterclaim? Was that an offer the adequacy of which the Judge had to determine? In Coulson LJ's view, the answers to both those questions was no.

Coulson LJ also noted a potential wider point too, which was whether a payment into court is in principle a proper way in which security could be provided by the defendant, in the circumstances of an adjudicator's decision in favour of a claimant company in liquidation. It was not a mechanism that had ever been suggested, and therefore considered, in any of the authorities.

Coulson LJ said that an order requiring payment of such monies into court was the worst of all possible worlds. It was contrary to the underlying philosophy of construction adjudication because, instead of maintaining construction industry cash flow, it would deprive Erith – a working contractor – of cash, whilst leaving the money sitting uselessly in the court's account. It would also not be available for distribution by the liquidators of JDC, so it was difficult to see how it is of any benefit to them.

Coulson LJ went on to consider whether a company in liquidation was entitled to enter judgment on its claim arising out of an adjudicator's decision, without regard to the paying party's set-off and counterclaim? In *Bresco*, Lord Briggs explained how and why the commencement of an adjudication by a company in liquidation, and the determination of that claim in adjudication was not a futile exercise. Lord Briggs had further in mind that any enforcement would not be for the claim, but for the net balance after taking into account set-off.

Coulson LJ noted that it appeared that Lord Briggs' starting point was that summary judgment to enforce an adjudicator's decision would frequently be unavailable when the claimant was in liquidation, with the court either refusing it outright or granting an immediate stay of execution. Where the liquidator sought to enforce the adjudicator's decision summarily, there was a real risk that it would deprive the respondent of its right to have recourse to the insolvent company's claim as security for its cross-claim, and that in such circumstances the court would again refuse summary judgment.

The case here was not a case where the parties had agreed that the adjudicator would finally decide the net balance. Erith maintained a set-off and cross-claim saying that JDC had been overpaid, even before account was taken of the sum of £1.2 million identified in the Decision. That set-off and cross-claim had yet to be finally determined. Thus, in line with the insolvency set-off principles, there was no entitlement to judgment on the sum provisionally found due to the insolvent company.

Coulson LJ noted that JDC suggested that an insolvent claimant in adjudication enforcement should (subject to jurisdiction and natural justice arguments) always be entitled to summary judgment because adjudication was pointless without summary enforcement. That was untenable for a number of reasons. Primarily, it sought to rewrite *Bresco*. The Supreme Court's focus was on how and why an insolvent claimant should be entitled to commence adjudication proceedings. It was not directly concerned with enforcement at all. The provisional finding of an adjudicator, even on a single final account dispute where no other significant claims arose, could not be treated as if it were a final determination of the net balance, in circumstances where the other party maintained its set-off and cross-claim. It was not a question of security; it was a question of the insolvent company's cause of action being for the net balance only. There was no discretion because it is impossible to waive the Insolvency Rules.

So, whilst *Bresco* did allow for insolvent companies to adjudicate, there remain a number of hurdles to overcome, before enforcement of any award, including that the terms of any security must be clear, unequivocal, and free of exemptions.

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