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Welcome to the December 2015 edition of *Insight*, Fenwick Elliott's newsletter which provides practical information on topical issues affecting the building, engineering and energy sectors.

This issue considers the new guidance that has been provided by the Court of Appeal in relation to final accounts, and the practice points arising.

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New Court of Appeal guidance on failure to serve payment and payless notices

On 1 December 2015, the Court of Appeal provided for the first time authoritative guidance on the practical effect of any failure to serve payment notices and payless notices in response to applications for payment in the context of contactor's termination accounts in its decision in Matthew Harding (t/a MJ Harding Contractors) v Paice and another [2015] EWCA Civ 1231.

The purpose of this 54th (and final) issue of *Insight* of 2015 is to consider the new guidance that has been provided by the Court of Appeal in relation to final accounts, and the practice points arising.

Over the course of the past year, three cases[1] have come before Mr Justice Edwards-Stuart presenting the all too familiar scenario whereby the contractor notified the sum due in a payment notice, and the employer failed to serve either a payment notice of its own, or a payless notice.

Harding v Paice

The facts

Mr Paice and Ms Springall (together "*Paice*") were property developers who engaged MJ Harding ("*Harding*") to carry out residential works to two properties in Surrey under a JCT Intermediate Building Contract 2011 (with amendments) ("*the Contract*") in March 2013.

Work commenced the following month, but the relationship between the parties quickly deteriorated and Harding gave notice to terminate the Contract in January 2014. The contractual termination provisions provided that

(i) Harding was required to submit a final account in respect of work it had carried out, including the total value of the work properly executed up to the date of termination (under clause 8.12.3);

(ii) Paice was to pay the amount that was "properly due" in respect of the account within 28 days of submission of its final account (under clause 8.12.5); and

(iii) Paice had the option to commence adjudication or litigation proceedings within 28 days of the issue of the Final Certificate, in which event the Final Certificate would cease to be conclusive (under clause 1.9).

Paice failed to pay Harding's final account, and Harding commenced adjudication proceedings. Harding claimed it was entitled to the sum due in its final account, which became the sum *"properly due"* under clause 8.12.5 of the Contract as Paice had not served a payless notice. Paice issued counter-adjudication proceedings in an attempt to re-value Harding's final account, and Harding applied for an injunction in an attempt to prevent Paice's counter-adjudication proceeding. In its injunction proceedings, Harding argued the failure by Paice to serve a valid payless notice made the sum in its final account the sum that was "*properly due*" under clause 8.12.5 of the Contract. In the alternative, Harding asserted that the substance of its final account had already been referred to adjudication and could not therefore be revisited.

Decision at first instance

Briefly,[2] Mr Justice Edwards-Stuart noted the adjudicator had proceeded on the basis that if Paice wished to pay less than the sum of Harding's final account, it was obliged to serve a valid payment notice, in default of which, Paice was committed to the amount stated in Harding's final account.[3]

In the instant case, Mr Justice Edwards-Stuart highlighted that clause 8.12.5 was slightly unusual, because unlike the interim payment machinery in the Contract, it required the employer to pay the amount "*properly due*" in respect of the final account; it did not require the employer to pay the amount stated in the final account, as this would operate to prevent the reckoning process that is inherent in final accounts taking place.

Mr Justice Edwards-Stuart found the adjudicator's decision in the context of the final account to be incorrect, as it would deprive the employer of the right forever to challenge the contractor's final account. Taking the worst case scenario, if the contractor had overvalued its final account, the contractor would receive a windfall

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to which he was not in fact entitled, and more importantly, which the employer could never recover.

Applying this finding to the facts, Mr Justice Edwards-Stuart held that the adjudicator had not, as a matter of fact, determined the amount that was "*properly due*" to Harding under clause 8.12.3, as a result of which Harding's case failed at first instance on the facts.

Issues on the appeal

Harding appealed to the Court of Appeal on two issues. The first was whether the adjudicator had jurisdiction to decide the dispute because it was the "*same or substantially the same*" as that which had already been decided, as the adjudicator had already decided the "*amount properly due*" in respect of the final account. In the event the adjudicator had not decided the "*amount properly due*" (because his finding centered on the absence of a payless notice), whether he had still been asked to (and did) decide that issue.

The second issue before the Court of Appeal was whether paragraph 9(2) of the Scheme was engaged, which provides an adjudicator must resign when the dispute is the same or substantially the same as one which has been referred to adjudication, and in respect of which a decision has already been made.

Decision of the Court of Appeal

Taking the latter issue first, Lord Justice Jackson, delivering a unanimous judgement, commented that it was quite clear from the authorities that the dispute (or disputes) that are referred to a first adjudicator should not be looked at in isolation: what the first adjudicator decided also has to be considered. Once this aspect has been examined, it can be determined how much (or how little) remains available for consideration by a later adjudicator. Applying this to the facts, Lord Justice Jackson found that as a matter of construction, the word "decision" in paragraph 9(2) of the Scheme means *"decision in relation to that dispute"*.

As for the first issue, although the adjudicator had reached a decision in relation to the failure to serve a payless notice (which was a contractual issue), he had not reached any decision in relation to the value of the final account, (which was a separate valuation issue). Accordingly, the valuation issue could properly be dealt with by a later adjudicator. In practical terms therefore, the employer's failure to serve a valid payless notice meant the employer had to pay the full amount shown in the contractor's account, and (in the words of Lord Justice Jackson) "*argue about the figures later*".

In his judgment, His Lordship emphasised it was not necessary to undertake a detailed analysis of the decision of Mr Justice Edwards-Stuart in *ISG Construction Ltd v Seevic College* (which concerned a failure to serve a payless notice in the context of an interim account), but there were a few pertinent points that were worthy of mention. It was Mr Justice Edwards-Stuart's finding that if an employer fails to serve the relevant notices, it must be deemed to have agreed the valuation stated in the relevant interim application, and that accordingly, the adjudicator must be taken to have decided the question of the value of the work carried out by the contractor for the purposes of the interim application in question.

What is crucial to note is that Mr Justice Edwards-Stuart made clear that the agreement as to the amount stated in an interim application (and therefore, the value of the work on the relevant valuation date) could not constitute any agreement as to the value of the work at some other date. In practice therefore, it is not open to an employer to bring a second adjudication to determine the value of the work at the valuation date of the interim application in question, but there is nothing preventing the employer challenging the value of the work at the next application, even if he is arguing for a figure that is lower than the unchallenged amount stated in the previous application.

Lord Justice Jackson emphasised that there is a crucial difference between *ISG Construction Ltd v Seevic College* (which relates to interim accounts) and *Matthew Harding (t/a MJ Harding Contractors) v Paice and another* (which relates to final accounts). In the case of final account following termination of the Contract, clause 8.12.5 requires an assessment of the amount which is "*properly due in respect of the account*", and expressly permits a negative valuation. Notably, Lord Justice Jackson declined to comment on the position in relation to interim applications on the basis that special conditions apply to interim payments. He was not specific on this point, but commented that mistakes can be put right at the next payment application.

Practice points arising

- Following the decision of Lord Justice Jackson in the Court of Appeal in *Matthew Harding (t/a MJ Harding Contractors) v Paice and another*, in the case of contracts such as the JCT one here, the payment amount for termination final accounts is the sum which is "*properly due*" in respect of the final account, irrespective of the service of any payless notice.

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- Following the decision of Mr Justice Edwards-Stuart at first instance in I*SG Construction Ltd v Seevic College* [2014] EWHC 4007 (TCC) (as clarified by Mr Justice Edwards-Stuart in *Galliford Try Building Ltd v Estura Ltd* [2015] EWHC 412 (TCC)),[4] the position currently in the case of interim accounts is that the amount of the interim payment is the sum which is stated to be due in the interim payment application, and any necessary adjustments can be dealt with at the next interim payment application.

Conclusion

The judgment of the Court of Appeal in Matthew Harding (t/a MJ Harding Contractors) v Paice and another is notable not only for what it decided, but also for what it declined to decide.

Although Lord Justice Jackson provided authoritative guidance in relation to final termination accounts, he stopped short of providing any additional guidance in relation to the position in relation to interim payments. Interim payments are currently dealt with by the first instance authority of Mr Justice Edwards-Stuart in *ISG Construction Ltd v Seevic College* [2014] EWHC 4007 (TCC) in which the court held an employer's failure to serve a payless notice in relation to an interim account would not prevent it from commencing later adjudication proceedings to determine the value of the works as at the date of the interim payment application.

Whether the Court of Appeal would follow the same reasoning as Mr Justice Edwards-Stuart in I*SG Construction Ltd v Seevic College* [2014] EWHC 4007 (TCC) if it is called upon to revisit the position in relation to interim accounts remains to be seen. For the time being at least, the position regarding interim payments and final accounts is inconsistent in regard to compliance with notice provisions. It should also be noted that the Scheme makes no such distinction between interim and final payments.

In the case of interim payments, there is a very strict requirement to comply with the contractual obligation to serve a payless notice. In the case of final accounts, the failure to serve a payless notice (in breach of contract) is not fatal on the basis that termination is a valuation issue, not a contractual issue, albeit this does not rest easily with the contractual notice provisions. Whether the courts will again be troubled by the distinction between interim payments and final termination accounts next year, and if so, the approach that will be taken, remains to be seen.

In the meantime, we wish the readers of *Insight* a Merry Christmas and a prosperous 2016.

Should you wish to receive further information in relation to this briefing note or the source material referred to, then please contact Lisa Kingston.
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Footnotes

1. *ISG Construction Ltd v Seevic College* [2014] EWHC 4007 (TCC), *Harding (t/a M J Harding Contractors) v Gary George Leslie Paice Kim Springall* [2014] EWHC 3824 (TCC), and *Galliford Try Building Ltd v Estura Ltd* [2015] EWHC 412 (TCC).
2. The decision of the court at first instance is dealt with in detail in the 42nd issue of *Insight* (http://www.fenwickelliott.com/research-insight/newsletters/insight/42).
3. Incidentally, Mr Justice Edwards-Stuart followed the same line of reasoning in his judgment in *ISG Construction Ltd v Seevic College* [2014] EWHC 4007, albeit that decision concerned an interim account, not a final account. See further the 42nd issue of *Insight*, *supra*.
4. As to which, see the 49th issue of *Insight* at http://www.fenwickelliott.com/research-insight/newsletters/insight/49.