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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.

Issue 279 – September 2023

Dispatch

Case Update: interpreting contracts

Lagan Construction Group Ltd (In Administration) & Ors v Scot Roads Partnership Project Ltd & Anr

[2023] ScotCS CSIH_28

We discussed this case in Issue 271. Lagan and the Second Defender formed a Joint Venture to carry out motorway upgrade works for Scot Roads. Clause 5.5.6 of a letter of credit procured by Lagan provided:

> *"Project Co [Scot Roads] shall return to the Contractor by transfer into a bank account specified by such Contractor, an amount equal to such Contractor Company Contractor Security Account Balance as soon as reasonably practicable following: [two events] ..."*

One of the two events having passed, the issue for Lord Baird was what (or who) was meant by "the Contractor" in the first line; the JV or Lagan? The balance of the monies, after deduction of sums due to Scot Roads, was just over £1 million. If "the Contractor" meant Lagan, the parties were agreed that it was entitled to payment of the sums. If not, then a full hearing would be needed to determine what should happen. Lord Baird held in favour of Lagan.

On appeal, Lord Carloway noted that the litigation concerned the construction of a contractual provision containing a defined term. The clause stated that certain monies are to be returned to "the Contractor". The contractor was defined as a JV between the pursuers and the second defenders. The first defenders had paid the monies to that JV. Lagan maintained that they should not have done so. Lagan said that "the Contractor" should be construed as referring solely to themselves, i.e., Lagan.

Lord Baird had noted that the contract was not "*happily*" drafted, whilst Lord Carloway noted that the contract had some 80 clauses and 26 schedules (some "*not used*"). It was over 200 pages long, with over 30 pages of defined terms. It had: "*the air of being stitched together from similar contracts, rather than being bespoke*". All parties had legal advice and there had been some 21 earlier versions.

Two defined terms were at the core of the dispute. First, "the Contractor" was said to be the JV; second, as a defined term (clause 1(1)), "Contractor Company" meant "*any company forming part of the Contractor*". It was made clear that "Contractor" and "Contractor Company" meant different things for the purposes of the contract.

The contract required that the Contractor "*procure that each Contractor Company shall perform its obligations*" and that the Contractor shall deliver to Project Co an "*Acceptable Letter of Credit procured by each Contractor Company in favour of Project Co*" in a particular form. These letters were designed to ensure that the contract works were carried out and any defects either remedied or compensated for.

Both Contractor Companies obtained Letters of Credit, but Lagan went into administration. This resulted, under the JV agreement (clause 6.7), in Lagan's exclusion from further participation in the management and profits of the JV; albeit they would continue to be liable to share any losses. Project Co insisted on payment of the Letter of Credit sum into the account and that was done by the bank. In due course (20 June 2020), the "Letter of Credit Discharge Date" arrived. This triggered the application of the clause before the courts.

Lord Carloway noted that Lord Baird had asked whether the language of clause 5.5.6 admitted two possible constructions. If it did, it was only then that the court could have regard to commercial common sense as suggested by Lagan. If there was only one possible meaning, then the court would have to give effect to that meaning, even if that appeared to be commercially undesirable. From a commercial common sense point of view, the purpose of the account was to provide security for Project Co. Each Contractor Company had an obligation to the bank, which had provided the Letter of Credit, to account for the balance. It did not make sense to pay the balance to the JV, which had no such obligation. This would enable the second defenders to "*scoop the jackpot*", even if funds had not arisen from any default by the pursuers. Had both Contractor Companies become insolvent, it would make no sense for the funds to be retained by the JV but for the funds to be returned to the person who had an obligation to account to the bank.

Lord Carloway held that the parties' intention was most obviously gleaned from the language which they had chosen to use. The court should not normally search for what were termed "drafting infelicities" in order to justify a departure from the natural meaning of that language. A court:

> *"should identify what the parties agreed, not what it thinks that common sense may otherwise have dictated. Contracts are made by what people say, not what they think in their inmost minds".*

Lord Carloway agreed that Lord Baird was correct when he acknowledged that the clause began in an unambiguous manner. It stated that Project Co were to return the monies to "the Contractor" by transferring an equivalent sum into a bank account specified by "such Contractor". The "Contractor" was the JV. It was expressly not the component companies, each of which is defined instead as a "Contractor Company". The terms were used carefully throughout, and legal advice had been taken. There was no ambiguity and thus no basis to a search for an alternative meaning. The appeal was allowed.

Where there is an agreement between two persons, one of whom is a JV, and surplus funds exist at the end of the contract, the obvious consequence is that those funds be returned by the party holding them (Project Co) to the other party, i.e., the JV. What might happen to them thereafter is something which ought to be regulated by the JV agreement between the Contractor Companies.

Adjudication: true value adjudications

Henry Construction Projects Ltd v Alu-Fix (UK) Ltd

[2023] EWHC 2010 (TCC)

Henry applied for summary enforcement of an adjudicator's decision in the sum of £190k. Alu-Fix said that the starting by Henry of the true value adjudication ("TVA") before payment of a notified sum pursuant to s.111 of the HGCRA meant that the adjudicator did not have jurisdiction. Henry said that the point was a novel one, and was not a jurisdictional point, as such. Rather, Henry should be allowed to rely upon the decision in the TVA, having paid the immediate payment obligation consequent upon the decision of a previous adjudicator in the prior "smash and grab adjudication" ("SGA"), which followed the raising by Henry of a "genuine dispute", namely asserting the validity of two pay less notices ("PLN") following Alu-Fix's payment application ("PA").

The contract was a JCT Standard Building Sub-Contract. Alu-Fix made a PA on 15 November 2022 in the sum of £257k and then referred the non-payment to the SGA on 15 December 2022. Henry said there were two valid PLNs, and then, on 18 January 2023, commenced the TVA. The SGA was ongoing. Alu-Fix invited the TVA adjudicator to resign. The TVA adjudicator noted that:

> *"2. As things currently stand, the question of whether there is an undischarged primary payment obligation is in dispute and is the subject of the [SGA] adjudication...As such, presently there is nothing preventing me from proceeding.*
>
> *3. In the event [the SGA adjudicator reaches a Decision that there has been a failure to pay a notified sum, then I accept that, unless and until a Court decides that such Decision is not valid, it will be binding on the parties. In such circumstances, I accept that, unless that payment obligation is discharged, it would not be appropriate for me to proceed. However, we are not in that position yet".*

The SGA decision was issued on 27 January 2023 in favour of Alu-Fix. The TVA adjudicator stayed the TVA pending payment, confirming that they would resign if payment was not made in accordance with the decision. Henry made full payment on 2 February 2023 and the TVA stay was lifted.

DJ Baldwin referred at length to the decision of O'Farrell J in the case of *Bexheat v Essex Services Group* (*Dispatch*, Issue 263) and the Judge's conclusion that:

> *"(i) where a valid application for payment has been made, an employer who fails to issue a valid Payment Notice or Pay Less Notice must pay the 'notified sum' in accordance with s.111 of the 1996 Act;*
> *(ii) s.111 of the 1996 Act creates an immediate obligation to pay the 'notified sum';*
> *(iii) an employer is entitled to exercise its right to adjudicate pursuant to s.108 of the 1996 Act to establish the 'true valuation' of the work, potentially requiring repayment of the 'notified sum' by the contractor;*
> *(iv) the entitlement to commence a 'true value' adjudication under s.108 is subjugated to the immediate payment obligation in s.111;*
> *(v) unless and until an employer has complied with its immediate payment obligation under s.111, it is not entitled to commence, or rely on, a 'true value' adjudication under s.108".*

Henry said that the case here differed from those previously decided, in that, at the time that the TVA started there was an ongoing "genuine dispute" as to the validity of the PLN of 25 November 2022. Therefore, unless and until there was an adjudication that there was no valid PLN, no "immediate payment obligation" arose. Accordingly, the embargo on launching a TVA prior to the payment of any immediate payment obligation was not engaged and no question of jurisdiction could arise. The payment obligation became immediate upon the ruling of the SGA adjudicator and that was discharged within the deadline ordered. Henry further said that it could not be right that there might be a nil finding on a valid PLN, but that the TVA nevertheless had to await that outcome before being commenced. A decision in Alu-Fix's favour would be a huge curtailment on "employers'" rights, especially given that prompt payment of the SGA decision had been made.

Alu-Fix said that a TVA could not be started whilst there remained an unsatisfied immediate payment obligation. The adjudication process was speedy in any event, even without being able to start before the outcome of any SGA. Any immediate payment obligation must be paid to assist with cashflow. The burden was on Henry to either pay upfront, before commencing the TVA or, alternatively, on choosing to raise a dispute, to accept that the TVA will inevitably be delayed.

DJ Baldwin said that the key element here was the determination of the commencement date of the immediate payment obligation. If this date was, or was to be treated as being, before 18 January 2023, then Henry was not entitled to commence the TVA and, therefore, the TVA adjudicator could not be said to have had jurisdiction. As the TVA was prematurely commenced, it would be a nullity. Here, the SGA adjudicator decided that the final date for payment was 13 December 2022. The Judge could not see any basis for concluding anything different. This was finding the facts as they always existed, and applying them to the question of the existence of jurisdiction. The result was that Henry was not entitled to commence the TVA on 18 January 2023 without first having discharged its immediate payment obligation.

The Judge made clear that the outcome here was not closing the door on commencing a TVA prior to the outcome of an SGA. Whilst it ought to discourage such a course in areas of spurious SGA disputes that should not deter those who have a sufficient level of confidence that any dispute raised should result in a finding that there was no immediate payment obligation. The the difficulty with Henry's submission was that it would risk tipping the balance unfairly towards the disputing party and prejudicing the ultimately vindicated right of the payee to be paid. In other words, the disputing party could not only delay paying what might ultimately, as here, be decided to be a sum which was already due, but also would be able to steal a march on the other party by being permitted to commence a TVA when the notified payment should have been made all along. If there is a genuine dispute as to the notified sum, the payer has the ability to protect itself by issuing a valid PLN.

Dispatch is produced monthly by Fenwick Elliott LLP, the leading specialist construction law firm in the UK, working with clients in the building, engineering and energy sectors throughout the world.

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