Centra News

Centra Consult LLP
Dispute resolution, claim preparation and delay analysis

October 2017 Volume 2, Issue 1

BIRTHDAY CELEBRATION

IN THIS ISSUE :

10 Year **Anniversary**

In recognition of our 10 year anniversary all of our friends and Clients are invited for drinks and canapes at the Speakeasy within the Voodoo Rooms (seemed apt!) at 19a West Register St, Edinburgh, EH2 2AA on the evening of Wednesday 1st November 2017 from 6.00pm to later. (See additional flyer).

Please RSVP to sandydickson@centra-consult.com

CHAIRMAN'S INTRODUCTION

A 10-year anniversary!

It is hard to believe that it is 10 years since Centra Consult LLP came into being. Despite my best efforts in that time we have grown into one of the largest specialist consultancies in Scotland for our particular areas of business.

Such an achievement is all the more remarkable given that some of our competitors are both international businesses and claim to be world leaders in their particular field.

I believe that our success stems both from the quality of our people and also from our clear understanding of the market in which we operate and the clients that we serve.

CHAIRMAN'S INTRODUCTION CONTINUED .....

Understanding what you are good at and what you are not so good at is a clear skill in itself. Making others understand what it is you are able to do for them and why it is of benefit to them is also a skill.

The various competing professions often think that what the other guy does is easy and/or is a bit of an 'add on' rather than a key element.

I often find that the 'quantum' element of a dispute or potential dispute is left to the last gasp. Quite often when investigating the quantum, you uncover the flaws in the case and that whatever the rights and wrongs that may be argued, the ultimate figure will be substantially different from that first mooted. It is often the case that the number involved will have a significant effect upon how a matter proceeds. A claim of £1M may well require significant input to manage it but if it is actually closer to £100K, there is a risk of the costs exceeding the value fairly quickly.

Similarly, delay analysis is simply a methodology of presenting facts in an understandable fashion. Trust me, it may not seem that way but that is all that delay analysis is. You may be familiar with the expression 'information is power'. Unfiltered information is simply confusion, the 'power' comes from the ability to filter information and present it in an understandable fashion.

Buildings are actually built by 'white van man', not Architects, Engineers, Surveyors, Lawyers, Managers or numerous others. An estimate is only a 'best guess', perhaps based on detailed information and perhaps not, which is converted into a fixed agreement via increasingly tightly written contracts allocating risk often to those least suited to manage it. Parties are then surprised when matters do not always go as planned (guessed/estimated). Hence, it is important to have a filter that understand what it is that it is filtering.

So, thank you for your support over the last 10 years and we look forward to assisting you over the next 10 years.

SOME THOUGHTS

I was thinking about reinventing the wheel, as it seems in this modern age the drive for improvement is the key to success (or so I am told). 'Smart' devices and 'smart' motorways will make all of our lives easier and more efficient (it is a pity about the quality of the operatives though). If the UK construction industry intends to have a future, it needs to go back to basics. The following is an extract from one of the recent trade magazines.

Building's list of the UK's Top 150 contractors and housebuilders paints a picture of an industry in probably its best shape for some years. Turnover for both contractors and housebuilders is up sharply, topping £100bn for the first time in the industry's history, while contractors saw their profit margins finally start to rise – slightly – after near constant decline since 2010.

However, while housebuilders are largely debt free and look in good shape to face whatever crazy political and economic mud is thrown at them in the year ahead (see Housebuilders – Strong and Stable, overleaf), for contractors it is only in comparison to the dire performance of the recent past that the picture seems positive. Carillion is still in place as the UK's second-biggest construction firm by total turnover, but the firm's profit warning – issued earlier this month, after this data was compiled – casts a long shadow over tables topped by a distinctly unhealthy first tier. Laing O'Rourke too, still the UK's second-biggest contractor by contracting turnover, remains on the sick bed, joined also this year by fellow top 10 players Kier and Interserve, while Balfour Beatty, reporting a profit margin of just 0.09%, is only slowly convalescing after four years on the operating table.

If these problems can beset the UK's biggest and strongest firms, then how much more perilous is the market for the smaller players with seemingly less balance sheet strength? And what do these figures say about the capacity for contractors to navigate the inevitable political and economic uncertainties of Brexit and the hung parliament?

Strong growth

First, then, the relatively good news. The turnover of the Top 150 housebuilders and contractors rose overall by 8.8%, from £92.1bn to £100.2bn. With many of the smaller firms outpacing their larger rivals, the average turnover growth for individual businesses was a very rapid 13%. And the growth was not centred just on housebuilders: contracting-led businesses grew at very nearly the same rate. That average also hides stellar performances from individual firms like Winvic Construction, which

WITH MANY SMALLER FIRMS OUTPACING THEIR LARGER RIVALS, THE AVERAGE TURNOVER GROWTH FOR INDIVIDUAL BUSINESSES WAS A VERY RAPID 13%

The results that Carillion eventually unveiled identified a loss of £850M, which says a lot about the industry never mind the company. In the dim and distant past, I worked for the conglomerate that was the Tarmac Group. They were at that time a good company to work for. There were a significant number of long terms employees, from labourer's to Directors, with 25+ years of service. Their capacity to build was significant and the breadth of experience and knowledge within the group was impressive.

In an effort to become more exciting (to the city I assume), they decided to become the biggest volume housebuilder in the UK. In that vision they succeeded but financially, it was not a great move for them.
In due course, they swapped their housebuilding with a rival and took on board the rivals quarrying and construction division, a greater result for the rival, not such a great result for Tarmac. Later, after a great deal of change and divestment, they morphed into Carillion.

The ultimate success can be gleaned from the figures that have just been released as noted above.

The Tarmac training school trained surveyors, engineers and managers at all levels in all aspects of the construction business. Every month, every surveyor and every site agent (as they used to be known) was dragged over the coals about progress and the financial position of each project and woe betide you if you were not on the ball. The agent was expected to have a complete grasp of the financial position of the project and the QS reported directly to the agent. The great rival at the time was Balfour Beatty and they were run along the same lines and in current times have had the same difficulties. With the reinvention of the wheel all of these tried and tested procedures changed and everyone became 'managers'.

I am not against progress, far from it but if Clients wish to have access to a competent pool of contractors for their projects, they have to pay the proper price, to allow people to be trained and allowed to take the time to carry out their tasks to the requisite standards. If all you do is cut corners all you get is cut corners. The Client is not always right, sometimes he is just a client and looking for a service from a professional and experienced provider.

On another not wholly unrelated matter, it is reported that a result of the Edinburgh Schools fiasco, the construction industry should be ashamed of itself. One of the suggestions is that as a result of the failures encountered the specifications and contracts should be tightened up. It will be interesting to see if white van man reads any of these tighter contracts and specifications. As my old dad used to say, if you want a job done properly, do it yourself. I never heard him say subcontract it to someone cheap & cheerful. You do not have to be a professor of Architecture or even a learned judge to understand why projects fail, uniquely complex assemblies are carried out in a field, in the rain by men working to a fixed price and a poorly developed design. Rocket science it is not, or man would never have got to the moon.

Still, it keeps me in a job.

WHAT'S NEW?

Our colleague Ana has graduated from Strathclyde University with an LLM (with merit) in construction law. An excellent result and well deserved.

Our colleague Peter is now a consultant to Centra Consult LLP, which allows him a bit more time for his motorbike and scuba diving, pehaps not both at the same time (although that would be interesting to watch).

MATTERS OF INTEREST

When I originally drafted this article, I had noted with interest that a new and revised version of the NEC suite of contracts was about to be unleashed on us. I had wondered if this would be an improvement or simply change for the sake of change. It seems that the changes are limited and of limited benefit. One might wonder if it was simply an exercise in revenue generation via the need to purchase the new versions.

In the meantime, some thoughts on the NEC

Several years ago, before the NEC forms were as widely used as they now seem to be, I had a conversation with someone who had very extensive experience of using this form of contract.

She said to me that the reason I had such difficulty in understanding the contract was because I was a Quantity Surveyor. Initially, this seemed to me to be an odd consideration but I now appreciate that she was in fact quite correct. If you approach NEC from whatever angle with a 'construction background' head on, you will fail to understand what it is all about and how it is intended to operate. It does not operate, nor is it intended to operate, in the traditional, 'wait & see' manner. Our entire legal structure that surrounds construction contracts is based around 'wait & see', hence any legal advice received on the outcome of the contract, is no more than a 'best guess'. Legal advice is usually based on

known principles, previous decisions, rules of contractual interpretation and the known attitude of judges to scenarios.

Perhaps the single greatest achievement of the NEC suite of contracts is that there is, despite its extensive use, a complete dearth of legal decisions and guidance on what any of it means and how it should be applied. The supporter of NEC will point to this and say this is proof that it is working and that it is clear and easily understood, whereas the critics may argue that no one wants to be the first making new laws, given the inordinate expense and risk that is involved in such an undertaking (I heard a TCC judge say that they are desperate to get their hands on an NEC contract case).

Since my original draft of this item, we have had a Court judgment,(Northern Ireland Housing Executive v Healthy Buildings (Ireland) Limited) which, in my view takes us full circle to the 'wait and see' situation. Whist there may well be perfectly legitimate reasons for this, in fact it will simply allow the PM to avoid making a decision until after he knows what the cost might be. So much for working together to manage the situation.

The NEC suite is a microcosm of the industry itself. Many thousands of contracts are carried out successfully, more or less to time and more or less to budget with the clients more or less satisfied. The projects that you hear most about are those that go wrong and the more horribly and expensive, the better. We know from experience that projects go wrong and that the terms of the contracts can be difficult to fathom and apply under such circumstances. So, is the NEC suite any better, given its extremely low legal profile?

Well no, is the short answer. The contract states and assumes (rather naively), that the parties will act as stated and in a spirit of mutual trust and cooperation. So, what happens if they do not act as stated?

The contract does not say – except in the case of a contractor's failure to identify a CE within a specified time period, which he should have identified, when he is penalised severely.

What happens if the PM & Supervisor do not act as stated in the contract – the contract is largely silent on this difficult and oft occurring issue. Why would either the PM or the Supervisor not act as stated in the contract? Perhaps because the contract requires them to take responsibility for their decisions in advance of events unfolding and for them to take responsibility for and account for 'risk' (which may or may not in time come to pass).

Life for the RE or CA was much easier in the past, when he could 'wait & see'. He could then report to the Employer (and his Employer) about what had happened and what he would do, rather than what he thought might happen, what the risks were and what he was committing the Employer to, in advance of anything happening.

Suppose a contractor manages to convince the poor PM into accepting a course of events that could happen (risk) and convinces him to pay (implement) for this speculative course of action.

A PM is going to have a fine time explaining to his PI insurers, when called upon to do so by the unhappy Employer, that he did indeed commit the Employer to a possible course of action, that did not in fact manifest itself in practice and that the contractor is fully entitled to the time and money implemented for events that never took place.

No doubt, if the events turn out to be significantly worse than anticipated, the PM will not hear from the Employer, having 'saved' the Employer money.

So, is it any wonder that the PM is often reluctant to act as stated in the contract and keen to sit on the fence or to wait for events to unfold before making a decision.

FURTHER MATTERS OF INTEREST

Over the last few years the law surrounding the interpretation of contracts has strayed from the sensible to the completely bizarre, culminating in my view, with a Learned Judge expressing the view that there was no limit to the amount of red pen that the Court could apply to a contract in order to make sense of it.

This was in a case where the two combatants had had the clear benefit of legal advisors when agreeing and negotiating the terms of the agreement. The learned judge was clearly of the view that something had gone wrong with the language and the agreement produced an absurd result…..for one of the parties.

It may well be the case that for most of my time at law school I was asleep but I do recall that when disturbed from my slumbers it was mentioned that taking commercial advantage of one another is the basis of the capitalist economies in which we operate. It was said at that time that it was not the role of the Court to extract a party from a bad bargain.

It seems that perhaps we have progressed around in a circle and arrived back to where we were several years ago and that the words mean what they say. This has manifest itself most recently in MT Hojgaard A/S v E.ON Climate and Renewables UK Robin Rigg East Ltd [2017] UKSC 59 SC.

The unfortunate effect of this case is that it has introduced both certainty and uncertainty for contractors (and others) in equal measure.

FURTHER MATTERS OF INTEREST CONTINUED....

Certainty, in that the Courts will apply the words as written to give effect to the whole of the contract. That, at least is very welcome, the purpose of the commercial court was to give 'men of business' certainty in their dealings.

Uncertainty, in that this particular case involved the matter of defective grout in a wind farm. The Contractor used the 'standard' as set out in the contract, it seems that the 'standard' had a problem, which is now known about. The contract required a 20-year life span, which the applied grout was clearly (with the benefit of hind sight) not up to the job. So, could the contractor rely upon having used the specified product? Well, this went all the way to the Supreme Court who overturned the decision of the Court of Appeal and ultimately said that the Contractor was liable for the failed grout despite it being specified.

Sensibly, this should sound the death knell for 'D&B' style of contracts as the risks for the contractor are simply not worth the reward.

I doubt it will make the slightest difference to many, who are simply chasing work.

In a similar vein in my view is the recent decision of Imperial Chemical Industries v Merit Merrell Technology Limited [2017] EHWC 1763 (TCC).

If you have a few spare hours, it is well worth a read, it is a sorry tale of the construction industry summed up by an observation from the Judge on the evidence being put to him: as a witness was, in my judgment, highly unsatisfactory.

It seems to me from the judgement, that the Employer's position was, when their project went wrong, through no fault of the contractor, to seek to put the contractor out of business in order to minimize their own cost exposure.

So not only may a contractor be asked to take on unfathomable risks, even when the fault sits with the Employer, there is a risk that the Employer may seek to simply starve you out in a siege mentality rather than deal with matters in a professional manner.

Unless the Contractor has the time and the wherewithal to check all of the design and all of the specification and be certain of winning the work, why on earth would they contemplate taking on a 'D&B style of contract unless the potential rewards were very significant?

PAYMENT PROVISIONS

We are still seeing a number of Adjudications on the matter of payments, so here are some thoughts from my colleague Michael Neill:

Payment Notices & Applications for Payment

Practical Considerations for Contractors & Subcontractors (& others)

1. INTRODUCTION

One of the key issues that has left a mark on the construction industry over the last few years has been the emergence of a number of legal cases concerning payment notices and applications for payment. Consequently, it is widely acknowledged that this has led to an increase in the number of Adjudications on similar issues as parties attempt to utilise these judgements to their advantage.

Anecdotally, the RICS confirm that this is still, by far, the largest source of Adjudication disputes between contracting parties. It is therefore appropriate for parties to carefully reflect on their understanding of the current position.

No Contractor/Subcontractor or certifier should by this time be in any doubt about the consequences of:

- failing to submit a payment application on time
- failing to submit a payment application in the appropriate detail
- failing to identify an application for payment as an application
- failing to respond to an application for payment, whether a sum id due or not
- failing to issue a Payless Notice, if required

- failing to have sufficient provisions to ensure payment throughout a potentially extended contract period
- failing to comply with any prescriptive requirements in the relation to the content/style & submission of application.

Experience indicates that this is clearly not the case and with current Adjudication fees ranging between £150 to £350hr+, it can be an expensive hobby to fight an already lost battle – so be warned.

For the purposes of the above issues the cases of particular significance include:

- ISG v Seevic - December 2014
- Caledonian v Mar - June 2015
- Henia v Beck Interiors – August 2015
- Jawaby Property Investments v The Interiors Group – March 2016
- Bouyges (UK) Limited v Febrey Structures – June 2016
- Grove Developments v Balfour Beatty – October 2016
- Kersfield Developments v Bray & Slaughter – January 2017
- Surrey & Sussex Healthcare NHS Trust v Logan Construction – January 2017

The purpose of this article, therefore, is to consider some of the challenges that contractors can face when administering the payment provisions of construction contracts.

Put simply, the common law position is that the risk of unforeseen ground conditions rests with the contractor. Unless a contract makes specific provision for additional time and/or money in the event of unforeseen ground conditions then the risk remains with the Contractor.

2. KEY ISSUES

Payment Applications & Payment Notices

The ISG judgement in late 2014 arguably lit the torch paper for much of what has followed. In brief, this case reinforced the payment provisions of the Construction Act, as amended by the 2009 revisions.

This case demonstrated the serious consequences that can arise when parties fail to issue effective payment or payless notices. In this Instance, the consequences were that Seevic had to pay ISG the total value of their payment application. This amount was far in excess of what Seevic believed the true value to be. Unfortunately for Seevic, due to the lack of a payment notice, ISG's application acted as a default payee notice which had the effect of determining the value of the work.

In Caledonian v Mar, Caledonian referred their case to adjudication on much the same basis as ISG had done. Namely, that in the absence of an effective payment / payless notice from Mar, they were entitled to full payment of their application. In the first instance the adjudicator agreed with Caledonian and their reference to the ISG judgement. However, at enforcement stage the Judge disagreed and did not enforce the decision.

The peculiarities in this case, which distinguished it from the ISG decision, was the format and precision (or lack of) in which Caledonian submitted their payment application. The judge considered that Caledonian had departed from the format of their previous 14 payment applications. The judge considered that these payment applications were clear in their intent, clearly set out and submitted in accordance with the appropriate contractual dates. The payment application that was referred to Adjudication was merely an email, which referred generally to the account and did not, in the judge's view, meet the criteria of an effective payment application. Particularly, when he compared it to their previous submissions which were unambiguous in their presentation.

In this case you can detect that the judge is trying to redress the balance of the smash & grab culture that many consider has developed since the ISG case. Notably, he refers to the increased number of smash & grab cases and stated that "If Contractors want to benefit from these provisions, then they are obliged to set out applications / notices with sufficient clarity". The 2016 case of Jawaby Property Investment v The Interiors Group and the 2017 case of Surrey & Sussex Healthcare NHS trust v Logan Construction further reinforced this position.

The case of Henia v Beck brought the precision in which contractor's submit their payment applications under further scrutiny. Beck argued that an application for payment which they submitted 6 days late, automatically fell into the next available valuation period. Subsequently, when Henia failed to issue an adequate payment notice, Beck sought full payment of their application. The judge disagreed with Beck on the grounds that their application for payment was not valid.

It was clear that this application was intended for the end of April 2015 and was submitted late. It also included no cognisance for works carried out until the end of May 2015 which reinforced the view that it was, in reality, a valuation for works up until the end of April 2015. The inference being that Beck should have issued a fresh application at the end of May 2015 which should have been clearly labelled in its intent.

Payment Cycles & Dates

The 2016 the case of Grove Developments v Balfour Beatty highlights the dangers that can occur when projects overrun and there is no contractual provision for interim payment beyond practical completion. In this case, the court decided that Balfour Beatty was not entitled to further monthly payments after the date of practical completion. This was because, in the courts view, the contract was compliant with the Construction Act and therefore Balfour Beatty could not rely on the scheme for construction contracts to rescue them.

The parties would have course been free to agree an extension to the payment cycles, however, in situations where relationships breakdown then this agreement may not be forthcoming.

When agreeing on the terms of building contracts, parties should take cognisance of this and ensure that adequate provision is made for interim payment beyond the contractual date for practical completion.

A further case in 2016, Bouygues (UK) Ltd v Febrey Structures Ltd, demonstrated the care that must be taken when drafting and operating the payment provisions of contracts. In this instance, the court found that there was a clear error in the payment schedules which rendered them non-compliant with the Construction Act. When Bouygues (The main contractor) tried to rely on these dates for the purposes of issuing Payment Notices, the court found them to be invalid which resulted in Febreys (Subcontractors) payment application / notice being considered valid instead.

3. PRACTICAL CONSIDERATIONS

It is clear that Payment Notices and Applications for Payment are intrinsically linked. It is essential that contractors establish appropriate templates at the start of a project and that the document is clear in what it claims to be. Notably, Contractor's should not depart from this format during the project if they truly expect to get paid.

As a minimum, a valid payment application should consist of the following:

- Letter (or covering email) stating that the document is an Application for Payment in accordance with the relevant contractual provisions
- State the period that the application relates to (i.e. state that the application relates to the value of the works up to & including the relevant date)
- State the gross amount due at the relevant date
- State the basis on which the valuation is calculated
- State the amount that that was previously certified
- State the nett amount due in the period
- State the date which the Employer is required to issue Payment / Payless Notices by
- State the date which the Employer is required to make the final payment by
- Served in accordance with the communication / notices clauses as stipulated in the contract.

Close attention needs to be paid to the contractual submission dates. Departing from these dates may affect the validity of the applications. The Henia v Beck case demonstrates that an application submitted late, may not automatically fall into the next available payment cycle. If a date is missed then it is advisable to establish the next correct date and resubmit with a clearly labelled and documented payment application. It would be unsafe to assume that adjudicators will award in favour of a pursuing party unless the intentions are clearly demonstrable.

There may be occasions when it suits both parties to operate out with the demands of the contract. Reasons for this could include operational time constraints / holidays / IT failure / continued negotiations on specific matters prior to finalising a payment certificate. Reaching agreements in the event of any of the above is entirely sensible. While co-operation between the parties should be encouraged, there are certain issues to consider such as:

- Accurately recording agreements to preserve rights and protections
- If you agree a revision to an application submission, the payment envelope can extend which may result in later payments which can have cash flow implications
- Communicate clearly to the other party whether the agreement relates only to one particular payment application and that future applications will continue to be dealt with via the contractual mechanisms.

As demonstrated in Grove Developments v Balfour Beatty, it is advisable to consider the provision of valuation dates beyond the contractual date for practical completion to avoid any unnecessary cash flow issues.

From a main contractor's perspective, dealing with the employer under the main contract is arguably the easier part. Things can get slightly more complicated when you introduce the contractors supply chain. On an average project, it would not be uncommon for a main contractor to enter into up to 50 sub-contracts. These contracts can range from the smallest of packages, designers appointments and multi million pound sub-contracts.

These are all construction contracts and will all be subject to the revisions of the 2009 construction act. They will also all be affected by the developments in case law as previously described. The burden for the contractor is that, in many instances these contracts will not all be procured on the same terms. More specifically they may not be procured on the same payment terms.

Some sub-contractors may be signed up to fortnightly payments, some on 28 days, and in some extreme cases 60-90 days. The key point is that the utilisation of different payment dates can place subtle differences on the corresponding dates that notices are required. This necessitates that the project commercial team need to be fully aware of what notices are due and when.

Sub-Contractors come in all shapes and sizes. The main contractor will therefore encounter a broad range of commercial approaches. These can include contractually aware organisations that will comply stringently with the contracted payment provisions. There will also be organisations that partially comply with the contract but are inconsistent. You will also get organisations that are contractually naïve and issue financial correspondence randomly and in a variety of formats.

It is key that the contractor identifies a schedule of relevant application / notification dates for all of the sub-contracts that it enters into. If and when Sub-Contractors deviate from the submission dates, the contractor should issue clear correspondence outlining the non-compliance and request that the valuation is re-submitted in the correct form or at the correct date. At the very least the contractor should outline how they are intending treating the submission to alleviate any interpretation disputes arising in the future.

The contractor should always be aware of the contractual position and administer notices appropriately. Also, as with the payments under the main contract with the employer, the contractor should be mindful of the need to accurately record any agreements with their supply chain that deviates from the contractual requirements.

4. SUMMARY

Hopefully the developments in case law has meant that employers, contractors & sub-contractors have refocused the manner in which they approach payment notices and payment applications.

Whilst the Caledonian v Mar and Henia v Beck cases went against the judgement found in ISG v Seevic, it would seem that this is because the judges considered that the pursuers were being opportunistic and the payment applications were in any event, not valid. It would appear though, that had the applications been valid, the judge would have found in favour of the pursuers. The upshot being, that if an application is valid and you don't issue a payment / payless notice then you can expect an adjudicator or judge to order full payment of the application for payment. The validity of otherwise of what is claimed as due, is not a relevant consideration as to whether or not the application is valid, you may easily end up overpaying by a considerable sum, simply by forgetting to respond appropriately at the correct time.

Whilst cases continue to emerge that will develop this area of law based on a variety of specific circumstances, the fundamental issue remains the same. That is, to adequately protect your organisation, great care must be taken to ensure that payment applications and payment notices are issued in the correct manner.

By now, no competent operator should be getting 'Notices' wrong by failing to issue same appropriately, whether that be notice regarding payment or notices in terms of conditions precedent. Practical experience shows this not to be the case, the industry seems to be slow learners.

Of course, it goes without saying that all of the above considerations apply to the Architects/Engineers & Quantity Surveyors seeking to recover fees from a recalcitrant client as well…..