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Legal developments in construction law

1. Failure to give parties a chance to comment dooms adjudicator's decision

To assess critical delay on a construction project, it was first necessary to establish a baseline programme, a process complicated by the fact that one had not been agreed. The adjudicator selected as a baseline programme one which not only was not contended for by either expert, but which both experts had given reasons for rejecting, and he made an award to the pursuer based on a critical date that was two days earlier than the date proposed by the pursuer. Neither that date, nor the consequences of selecting it as the critical date, was canvassed with the parties. Was that a breach of the rules of natural justice?

Noting that the courts will in general summarily enforce decisions of adjudicators, but that where an adjudicator is found to have acted contrary to the interests of natural justice, enforcement will be refused, the Scottish court drew, from the English and Scottish case law, these propositions, whose common theme is that the adjudicator's procedure must be fair:

- each party must be given a fair opportunity to present its case;
- if the adjudicator makes their own investigations and inquiries, or proposes to use their own knowledge and experience to advance significant propositions of fact or law not canvassed by the parties, it will normally be appropriate to canvas them with the parties before making a decision;
- the adjudicator should not decide a point on a factual or legal basis that has not been argued or put forward before them;
- but an adjudicator can reach a decision on a point of importance on the material before them, on a basis for which neither party has contended, provided that the parties were aware of the relevant material and the issues to which it gave rise had been fairly canvassed;
- for a breach of natural justice to vitiate a decision, it must be material; a breach is likely to be material where the adjudicator has failed to bring to the parties' attention a point or issue on which they ought to have been given the opportunity to comment, if it is either decisive or of considerable potential importance to resolving the dispute;
- an adjudicator is afforded considerable leeway and is entitled to adopt an intermediate position not contended for by either party without giving notice of their intention to do so.

The court noted that the line between an adjudicator going off on a frolic of their own and making legitimate use of their experience to analyse material which has been lodged, and commented on by parties, before reaching a decision not contended for by either party, is not always an easy one to draw, particularly when it is remembered that an adjudication decision reached by an adjudicator who has embarked upon the latter exercise will be enforced by the courts, even if wrong.

The court ruled that the adjudicator did not give the parties a fair opportunity to comment on his proposed selection of the baseline programme and the consequences he considered that had for the critical date and this failure was underlined by the fact that the adjudicator did not address the defender's time bar argument. The decision on the particular issue was vitiated by a breach of the principles of natural justice, and it could not stand.

VAN OORD UK LTD AGAINST DRAGADOS UK LTD [2022] ScotCS CSOH_30

2. Court reiterates pay first , adjudicate later, Construction Act principle

A subsubcontractor, BHL, obtained a 'true value' adjudication award against a subcontractor, ESG, in respect of its interim payment application 22. It then obtained a second adjudication decision that ESG had not issued a pay less notice in time and that BHL was consequently entitled to payment of the 'notified sum' in application 23, which was for a different valuation period, but with substantially the same items and figures as in application 22. In court proceedings by BHL to enforce the second adjudication award, ESG raised a number of challenges, including whether the 'true value' of application 23 was determined in the first adjudication, so that the second adjudicator had no jurisdiction, whether it was entitled, under a contract clause, to set off or make deductions against the second adjudication award, and whether it was entitled, under another contract clause, to have the 'true value' of the application in dispute determined by the same adjudicator at the same time as the 'notified sum' dispute.

Under the Construction Act a party who fails to issue a valid payment or pay less notice must pay the 'notified sum' by the final date for payment and, if they fail to do so, the receiving party can obtain an adjudication award in its favour. The paying party can embark on a 'true value' adjudication in respect of that sum, but only after it has paid it.

An adjudicator has no jurisdiction to determine matters which are the same, or substantially the same, in a subsequent adjudication but in this case the court ruled that the disputes or differences in the two adjudications were not the same, or substantially the same. The second adjudication award did not refer to the true valuation of application 23; it simply decided that BHL was entitled to payment in full by reason of ESG's failure to serve a valid pay less notice.

And ESG's argument that the 'true valuation' would be the same for both application 22 and 23, and binding on the parties, so that no further payment was due, had not been raised as a defence in the second adjudication. ESG was not entitled to rely on a challenge to jurisdiction in circumstances when it had failed to reserve its position on this matter.

ESG's argument that a contract provision entitled it to set-off, or make deductions, against the second adjudication award also failed, because it was contrary to section 8 of the Construction Act and the Scheme for Construction Contracts. An unqualified contractual right to set-off offends against the statutory requirement for immediate enforcement of an adjudicator's decision, as interpreted in the case law.

And another contractual provision, entitling ESG to refer more than one dispute to the same adjudicator (the 'notified sum' dispute and a third, true value, adjudication commenced by ESG in respect of application 23), was inconsistent with paragraphs 8 and 20 of the Scheme, which require the consent of all parties to a multiple dispute adjudication. The court noted that a difficult task could become impossible if one party could unilaterally require an adjudicator to determine a raft of disputes within one adjudication.

All the ESG challenges failed, as did an application for a stay of execution.

Bexheat Ltd v Essex Services Group Ltd [2022] EWHC 936

3. Co-insured under an 'all-risks' policy – but did that cover everything?

For the 2015 Rugby World Cup the RFU engaged a contractor to install ductwork designed by consultants and took out an all-risks insurance policy for the works. In proceedings against the contractor and consultants the RFU contended that there were defects in the ductwork which caused damage to cables when they were pulled through it. It was indemnified by the insurers under the policy in respect of the cost of replacing the damaged cables and related sums and claimed that the consultants and contractors were liable for those losses and the costs of rectifying the ductwork, because of defects in the ductwork design and deficiencies in workmanship. The contractor sought declarations, however, that it was a co-insured with the RFU under the policy and that

it had the benefit of the cover to the same extent as the RFU, so that the RFU could not claim against it in respect of the alleged losses covered by the policy and that the insurers could not make a subrogated claim against it in respect of the sum it had paid to the RFU.

In deciding preliminary issues, the court noted that the law does not allow an action between two or more persons who are insured under the same policy against the same risk. The consequence for subrogated claims by insurers, who have indemnified one co-insured, is that they cannot exercise subrogation rights against another co-insured who has the benefit of cover in respect of the loss or damage that would otherwise form the insurers' claim. These consequences only come into play when the relevant insurance is in place and the extent to which an insurer has, or does not have, subrogation rights is dependent on the terms of the relationship between the parties. The Supreme Court has confirmed that the rule is based on a term to be implied into the contract between the parties.

Applying the principles of agency, it is necessary to consider whether, and to what extent, the party effecting the insurance had authority to obtain cover for the other party and an intention to do so. The other party (e.g. contractor or sub-contractor) only becomes a party to the insurance if the employer or contractor was authorised and intended to contract on its behalf, and only to the extent of the cover which the employer or contractor was authorised and intending to obtain. Three cumulative conditions need to be satisfied for cover taken out by A to cover B's interest. A's authority must extend to making the insurance contract in question, A must have intended, when taking out the policy, to cover B's interests and the policy terms must not preclude extending coverage to B.

The court said that the case law is clear that, to determine whether, and to what extent, insurance cover applies to a contractor or sub-contractor it is necessary to look to the terms of the parties' contract, which provide the key to the existence and extent of the insurance cover. A person does not become a party to an insurance contract simply by reason of being named or identifiable as an insured, and when a person becomes a party as a consequence of the actions of another person then the terms of the contract between the insured party and that person govern the extent of the insurance.

Looking at the letter of intent issued by the RFU, the policy, and the JCT contract the position was clear. The effect of those documents and of the terms of Option C of the JCT contract was that the RFU was obliged to take out insurance which gave the contractor cover for physical loss or damage to the work executed or to site materials, but insurance in respect of the cost of rectifying damage caused by the contractor's own defective works was excluded.

If the parties had been contracting on the footing that recourse to the insurance would be the sole avenue for redress for damage of the kind which occurred then further amendments to the standard JCT contract could have been made to provide for that in clear and express terms, but that was not done, even though the contract was entered into three months after the policy was taken out. The court was satisfied that the agreement between the RFU and the contractor did not provide that, by taking out the policy, the RFU was creating a fund, recourse to which would be the sole remedy for loss suffered by the RFU as a consequence of breach or other default by the contractor. The Policy was effected on the basis that it was providing the cover contemplated by Option C in the JCT contract.

The Rugby Football Union v Clark Smith Partnership Ltd & Anor [2022] EWHC 956

4. Minister threatens action against construction product manufacturers over unsafe cladding

The Secretary of State for Levelling Up, Housing and Communities, Michael Gove, has written to the Construction Products Association about unsafe cladding.

He has instructed his officials to do 'whatever it takes' to make sure that construction product manufacturers are held to account through the powers in the Building Safety Act and says that his new recovery unit will pursue firms that have failed to do the right thing, including through the courts. He will also consider carefully how to use other powers to ensure there are significant commercial and reputational consequences for those firms that have not stepped up.

See: https://www.gov.uk/government/publications/letter-from-the-dluhc-secretary-of-state-to-the-construction-products-association-13-april-2022

5. Ban on ground rent charges in new residential leases starts on 30 June 2022

The Leasehold Reform (Ground Rent) Act 2022 which comes into force on 30 June 2022, puts an end to ground rents for new, qualifying long residential leasehold properties in England and Wales, except for retirement properties, where it will not come into force before 1 April 2023.

The very few exceptions from the Act are:

- applicable community-led housing;
- certain financial products; and
- business leases, defined by the Act as leases of commercial premises which include a dwelling, use of which substantially contributes to the business purposes.

Statutory lease extensions for both houses and flats remain unchanged and are therefore exempt from the provisions of the Act. For existing leaseholders entering into voluntary lease extensions after commencement, the extended portion of their lease will be reduced to a peppercorn.

The government will shortly publish guidance for consumers and enforcement authorities on the operation of the Act.

See: https://www.gov.uk/government/news/future-homebuyers-to-be-freed-from-expensive-ground-rent-bills-on-30-june

6. Government agrees funding of building safety repairs with major developers

The government has reached agreement with major housebuilders that they will fund and undertake, or procure at their own cost, as quickly as reasonably possible, all necessary remediation and/or mitigation work to address life-critical fire safety defects in all buildings in England of 11 metres and above that they have built or refurbished in the 30 years prior to 5 April 2022. They will also, to the extent they have not already done so, withdraw their buildings from, and/or reimburse, the Building Safety Fund and ACM Funds.

For details see:
https://www.gov.uk/government/news/agreement-with-major-developers-to-fund-building-safety-repairs

7. Building Safety Act receives Royal Assent

The Building Safety Bill received Royal Assent on 28 April. (See: Building Safety Act 2022 (legislation.gov.uk)).

Some provisions come into force on 28 June 2022, including the amendments to the Defective Premises Act, the new limitation periods that apply to the Act and section 38 of the Building Act 1984, provisions as to liability and limitation periods for construction and cladding products, building liability orders and remediation costs under qualifying leases.

See also: The Building Safety Act 2022 (Commencement No. 1, Transitional and Saving Provisions) Regulations 2022 (legislation.gov.uk)

The government's original timeline of July 2021, when the Bill was first introduced into Parliament, set out anticipated dates for elements of the Bill to come into force.

See: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/999356/Timeline_for_Transition_Plan.pdf

If you have any questions or require specific advice on the matters covered in this Update, please contact your usual Mayer Brown contact.

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