Construction Law Update

Summer 2016

Construction Dispute and Injunction to Restrain Winding-up Petition

In the recently reported case of COD Hyde Limited and Space Change Management Limited [2016] EWHC 820 (Ch) the Companies Court had to decide whether to grant the employer (COD) an injunction restraining the contractor (Space) from presenting a Winding-up Petition against it. The intended Petition was based on a Statutory Demand which referred to three unpaid interim applications for payment totalling around £680,000. The Contract was a bespoke JCT Design and Build Contract 2011 edition.

The application was refused.

The case illustrates that there are other weapons available to a contractor who is not being paid other than adjudication, in this case suspension, termination and the winding-up route. It also shows the drastic consequences that can follow if an Employer does not serve valid payment and payless notices.

Following non payment of its interim applications COD followed the contract procedure and gave notice of an intention to suspend performance of its obligation. The default in payment was not remedied within the 7 days and accordingly COD wrote to give notice of suspension and notice of default and they also wrote with a Statutory Demand.

It is worth remembering that the amendments to the Construction Act allowed a contractor to suspend part only of its obligations and gave the right to payment of costs and expenses arising out of the suspension. Exercising a right of suspension is something which contractors and sub-contractors might consider doing in the event of non payment rather than adjudicating.

Space Change then decided to terminate the contract as a result of non payment. By this stage it seems that COD had employed others to carry out their works in any event. COD attempted to argue that they were entitled to withhold payment until such time as a performance bond was put in place, but this argument was rejected and in the absence of valid payment notices or payless notices the COD were not entitled to argue that Space Change should not be paid. The Judge considered that COD did not have 'even a shadowy case' that there was a counter claim that exceeded the amount set out in the Statutory Demand.

An Employer rarely has a defence to a 'smash and grab' adjudication and the Technology and Construction Court take a robust view to adjudication enforcement and so an adjudication would certainly have been worth doing, but there may be good reasons why in this case, COD decided to go down the winding up route.

However in yet another case recently published, the Court dismissed the Respondent's Winding-up Petition as it found there was a dispute between the parties over whether the statutory payment mechanism as set out in the Construction Act and implied into construction contracts by the Scheme applied to the parties contract. In that case by applying for a Winding-up Petition in circumstances where there was such a dispute the Respondent found itself with two legal bills – its own and the applicant's bill which was summarily assessed at £13,750.00. The debt itself was only in the region of £6,500 and so whatever the tactical reasons for issuing a Winding-up Petition in this case, it may have been more cost effective to have referred it to adjudication. The case is Ro-Bal Steel Fabrications Ltd v Jones Site Services LH [2016] EWCH 292 (Ch).

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Duty of care even if you are not expecting payment

The Court has found that an architect and project manager who performed services for free owed duties of care in respect of the selection of the project team, the preparation of designs needed for pricing and construction, the exercise of costs control and periodic inspection of the works. The case of Burgess and Lejonvarn [2016] EWCH 40 is a reminder of the standard of conduct expected and required of professionals. In this case Mr and Mrs Burgess wished to have some substantial landscape works done to a high level design. The price of £150,000 had been quoted and Mrs Lejonvarn, an architect and project manager by trade and a friend of the couple considered this to be quite high. She offered to organise a team to carry out the work at a lower price and for the early stages of the project at least, she would not charge for her services as project manager. Unfortunately the project was a disaster and costs significantly overran. The relations between the friends soured and a claim is being made against Mrs Lejonvarn for £265,000 for the additional costs of carrying out the works without any professional indemnity insurance cover.

No contract existed between the parties but the judge concluded that a duty of care was owed in tort. The Burgess' relied upon Mrs Lejonvarn's professional expertise and she had accepted responsibility for a significant project. The relevant standard was that of a reasonably competent project manager and architect.

So the moral of the story is to be aware of the dangers of mixing work and friendship. Also, as a professional do not give advice without professional indemnity insurance and finally, the case demonstrates the importance of having proper contacts and appointments drawn up which set out each parties roles and obligations to each other.

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Contractors - who is in control?

As a client or a main contractor, would you expect to be liable for an accident to one of your contractor's employees when they have disobeyed a clear instruction? That is what happened when historic firm Josiah Wedgwood employed contractors at their warehouse in Stoke. They worked on the roof installing barbed wire and replacing skylights. Wedgwood then instructed them to not to go on the roof again. However, the contractors ignored this - a worker fell and was seriously injured

Wedgwood must have wondered why they were to blame, having issued a clear instruction. However, they had not truly integrated the contractors into their permit to work system. There should have been more supervision of the contractor's activities given the high level of risk (contractors are normally unfamiliar with the client's premises, safety rules and processes and therefore a greater risk to themselves and others). For this Wedgwood were fined £60,000 and the contractor £20,000.

The HSE guidance Use of Contractors – *a Brief Guide* (INDG368) and *Managing Contractors, a guide for employers* (HSG159 2nd edition 2011) discuss the appropriate level of checking by a client. In some cases, the client should not need to involve himself at all, for example if the job was a new build office. In others the contractors may be working alongside the client's employees and others for example refurbishing an existing workplace.

In such cases a number of statutory duties towards contractors could apply such as:

- Section 3 HSWA 1974
- Paragraph 11 MHSWR 1999
- Part 4 CDM Regulations 2015
- Paragraph 3 COSHH 2002
- Paragraph 3(3) Control of Asbestos Regulations 2012
- Occupiers' Liability Act 1957

Clients (and main contractors) should consider the six steps in INDG368 namely:

- Identify the job
- Select a suitable contractor - investigate experience, qualifications, memberships, arrangements for using sub contractors, previous accident/safety records. Inspect insurances, H&S policies, RAMS and training records.
- Assess the risks – sometimes this should be a joint exercise.
- Provide information instruction and training - contractors should be integrated into policies and procedures to the same level as the client's employees.
- Cooperate and coordinate.
- Consult – ie ask your staff how the contractors' work might affect their health & safety.
- Manage and supervise – a level of monitoring appropriate to the level of risk.

HSG159 lists five slightly different steps *Planning, choosing a contractor, Contractors working on site, keeping a check* and *Reviewing the work*. Although originally designed for the chemical industry HSG159 is the more detailed and interactive publication - containing a useful toolkit for assessing competence. Procedures for using contractors should be built round both sets of guidance.

Clients should also build health and safety requirements into their procurement procedures. Contractors should expressly acknowledge rules such as permit to work procedures and all this (including the contractor's responses to selection criteria) should be given contractual force. The right paperwork may help defend a claim or HSE investigation. Good selection and management of contractors may ultimately bring savings through greater efficiency. However most important of all is to avoid the nightmare scenario of a Wedgwood type accident. The answer to that is genuine engagement with contractors on health & safety. HSE guidance INDG368 and HSG159 provide a framework for achieving this. Anyone employing contractors in a risky setting should check their procedures measure up to the same standard.

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Joint seminar on Managing Asbestos Risk on Site and in the Workplace

Some fifty property, construction and insurance professionals met at the Gallagher Stadium, Maidstone earlier this year to hear from Jane Adamson, Founder and Managing Director of Adamson's Laboratory Services (ALS Envex) and Steve Dempsey of DMC Group Enabling Works Specialists and licenced asbestos removal contractors. Andrew Clarke health & safety law specialist at Gullands provided a legal overview and commentary on sentencing principles in asbestos prosecutions.

The seminar focused on managing asbestos risk on site and in the workplace, covering a number of subjects including:

- Responsibility of the dutyholder in non-domestic premises
- The employer's duties under the 2012 Regulations
- Providing adequate asbestos survey information
- Management of ACMs on your premises
- Distinguishing management and refurbishment/demolition surveys
- Managing asbestos removal on site

Guests were reminded of the requirement to keep documents under the 2012 Regulations up to date and review immediately where there has been a change in the premises or reason to suspect they are no longer valid.

Andrew Clarke comments: "When the duty to manage came into force 2004 there was estimated to be six million tonnes of asbestos contained in some 500,000 non domestic premises. With this level of asbestos still present in the built environment, asbestos risk management will be important for many years to come. Apart from fines and costs there is the cost of civil claims to bear in mind. We looked at how dramatic these could be if there is a contamination incident or an unplanned release of fibres.

If your business is affected by an asbestos legal issue call us for a free initial discussion. Andrew Clarke can be reached at a.clarke@gullands.com

Prosecuting "near miss" incidents and fines under new health & safety Sentencing Guidelines

Commentators are unanimous in predicting larger fines for health & safety offences following new sentencing guidelines effective from 1st February.

However, the guidelines are not just about bigger fines. They also require the Court to look at the risk of harm, not just the outcome. This means a minor injury or "near miss" which could have been fatal or cause life changing injuries will now attract a much higher fine than before.

Two "near miss" incidents have recently been sentenced. Conoco Phillips involved a fine of £3 million being handed out just days after the guidelines came into force. Conclusions about the new guidelines should not however be drawn as the case had been adjourned from 22nd January and the judge declared he was not bound by them. The judge sentenced the incident as a serious near miss in which he considered seven lives were put at extreme risk. The Defendant was an oil multinational with a turnover of £4.8 billion, so a large fine was called for even before the guidelines. The judge also did not need to rely on the guidelines to justify a big fine for a near miss, as it had already been decided in another case that a "Court does not have to wait until a death or serious injury has occurred to express its displeasure at wholesale breaches of the Defendant's responsibilities under the law".

However, the guidelines were very much in force when the second near miss case was sentenced on 8th April. Kent company *M J Allen Holdings* was fined £160,000 after a maintenance employee's foot slipped while he was working on crawling boards on a factory roof. Fortunately, the only injury was to the roof. However, the Court identified the obvious potential for death or life limiting injury and a medium likelihood of this occurring. This placed it in harm category 2 under the guidelines

Also sentenced in April were *C. Smith & Sons and Building and Dismantling Contractors Limited*. In that case CS&S contracted BDCL to dismantle a warehouse roof. BDCL employee Scott Harrower nearly fell through a skylight but managed to steady himself. The following day another workman did fall through a skylight, suffering multiple fractures. Police and paramedics attended, but amazingly work recommenced and hours later Mr Harrower fell 30 feet through another skylight, sustaining fatal head injuries. The proprietor of BDCL was jailed for six years for gross negligence manslaughter and fined £400,000 plus costs. The proprietor of CS&S was jailed for 8 months and fined £90,000 plus costs.

This case shows starkly why management should take a "near miss" just as seriously as a real accident, otherwise next time that is probably what it will be - and failing to act on previous incidents is likely to attract a high or very high culpability fine under the guidelines.

For a more detailed commentary on the sentencing guidelines please see our February article *New Sentencing Guidelines for Health and Safety Offences – Crime Should Not Pay* on the health & safety pages of our website www.gullands.com

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A buildings use, not who owns it critical to deciding VAT status

This isn't an area of law that has changed recently, but one which people do unfortunately get wrong with expensive consequences. The owners of commercial property will know that some building work can be standard rated or, if it meets one of the exemptions under the Value Added Tax Act 1994, it can be zero rated for VAT purposes, which can present a considerable saving when carrying out building and renovation work.

One of the qualifications for VAT zero rating is that the building is to be used for a 'relevant charitable purpose', however this should be approached with caution.

In a recent example, a charity renovated a listed property which it owned and it provided zero rating certificates to its building contractors, so they did not charge VAT on the building works. The building was not actually going to be used directly for the purposes of the charity that owned it, as it was going to be let to a private fee-paying school.

This came to light when one of the building contractors involved made contact with HM Revenue and Customs (HMRC) to check that it was in order for it to issue zero rated invoices for its work. HMRC stated that as the property was to be used as a fee-paying school, all invoices were to be standard rated. HMRC then wrote to the charity saying that it understood it had been issuing zero rating certificates to contractors and that these had been incorrectly issued.

The dispute went to a tax tribunal which ruled that although the lease was at below market rent and not intended to yield long-term profits, the property had been intended for use in the course of an economic activity.

This case serves as a reminder that before undertaking any building works, it is really important to establish the correct VAT rating, so it is charged at the standard rate or the exemption applied for, and your contracts should reflect this.

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David Brown recognised for his work

David Brown has been recognised for his work in the 2015 edition of The Legal 500 and has achieved a Band 2 ranking in the 2016 Chambers & Partners legal directory. David has recently been invited to talk at RICS CPD events.

Government reviews the use of retentions, does this mean changes for the Construction Industry?

The Department for Business, Innovation and Skills has recently announced a review of how retention arrangements work in the construction industry and the effect in particular on smaller businesses.

Retentions frequently cause issues in building contracts, although their use is widespread in other forms of contracts. In particular, the retention of money due for what can be a considerable period of time and which can be for a significant proportion of the total profit on a contract. This can cause serious cash flow issues for contractors and also their subcontractors.

There is also a widespread concern in the industry that the use of retentions imposes an unnecessary administrative burden on all parties. A retention may act as a practical guarantee for the quality of work done and materials used, but its payment is often in practice under the total control of the contractor's employer and may be unnecessarily delayed, or even be at permanent risk if the employer faces cash flow problems.

Some of the changes being suggested include the use of a bond system, or the use of payment into trust. Looking at the success of similar schemes used to protect the deposits paid by tenants of residential property shows how effective a simple change to the law can be.

Whilst the debate in the industry will no doubt continue, it will be too late for many businesses that continue to suffer from prolonged and overly excessive retentions, but getting the contractual terms right from the outset can often help to mitigate these issues as a construction job progresses.

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