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

This issue examines each of the decisions in turn and considers what can be learnt from them in practice.

Insight

Update on payment

Since we last looked at payment at the end of 2014 there have been three important decisions which have cast further light on the approach to payment (and adjudication) that is being taken by the Technology and Construction Court. *Galliford Try Building Limited v Estura Limited* [2015] EWHC 412 (TCC) looks at how work should be valued where no payment notice, default payment notice, payless notice or final certificate has been issued; *Caledonian Modular Limited v Mar City Developments Limited* [2015] EWHC 1855 (TCC) examines payment applications in the context of a final account settlement; and *Leeds City Council v Waco UK Limited* [2015] EWHC 1400 (TCC) deals with the validity of interim applications that were submitted both prior to and after the dates provided for by the building contract.

Galliford Try Building Limited v Estura Limited [2015] EWHC 412 (TCC)

The facts

Estura Limited ("Estura") engaged Galliford Try Building Limited ("Galliford Try") under an amended JCT Design and Build Contract 2011 ("the Contract") for the construction of the Salcombe Harbour Hotel in Devon. The contract contained Housing Grants, Construction and Regeneration Act 1996 ("Construction Act") compliant payment provisions and provided for interim payments to be made to Galliford Try in the usual way.

Near the end of the project, Galliford Try issued an interim application for £4m that it described as being an "indicative final account and valuation summary" ("the interim application") which came in at only around £4,000 less than the amount of the anticipated final account. Estura maintained that the sum due under the interim application was only £147,000 plus VAT, but it failed to serve a payless notice, as a result of which the £4m claimed by the interim application became the sum due.

Galliford Try initiated adjudication proceedings seeking payment of the Notified Sum and the adjudicator found in its favour. Estura then commenced a second adjudication seeking a declaration as to the true amount owing in respect of the interim payment application. The second adjudicator found that he had no jurisdiction in light of the decision of the first adjudicator, adopting the strict approach of the court in *ISG v Seevic*,[1] namely, that in the absence of fraud, contractors are entitled to the amount stated in their payment application regardless of the true value of the work in circumstances where the employer has failed to serve a valid payless notice.

Estura continued to resist making payment and later resisted enforcement on the basis that the decision of the first adjudicator was misguided, and contrary to the earlier decision of the court in *Harding v Paice*[2]. That decision provided that any failure by the employer to serve a payless notice would not be critical to its ability to challenge the contractor's final account, as this would create a very unfair situation whereby the employer would be prevented from challenging the contractor's final account for all time.

The decision

In arriving at his judgment, it was necessary for Mr Justice Edwards-Stuart to re-visit his earlier decision in *ISG v Seevic*, which was causing confusion. The Judge clarified that *ISG v Seevic* confirmed that a failure to serve a payless notice did not constitute an agreement as to the value of the work at some other date. In other words, whilst an employer's failure to serve a payless notice would prevent it from commencing adjudication proceedings to determine the value of the works as at the date of the interim payment application, it would not prevent the employer from challenging the value of the work at the next payment application.

Applying the Judge's reasoning to the facts of the case, Estura was entitled to certify a new notified sum upon receipt of the next interim payment application; it was not, however, entitled to challenge the sum claimed in Galliford Try's interim payment application. In light of this, Estura had no defence to Galliford Try's application for summary judgment and Galliford Try was awarded the sum claimed in its interim payment application.[3]

Practice points

- The decisions in *Harding v Paice* and *ISG v Seevic* (as we suggested in our last Insight on payment[4]) result from the way in which the JCT suite deals with interim payments and termination accounts.

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- In the case of interim payments, in the absence of a payless notice by the employer, the amount of the interim payment is the sum which is stated to be due in the interim payment application.
- In the case of final accounts, the payment is the amount which is "properly due" in respect of the final account, irrespective of any payless notice.

Caledonian Modular Limited v Mar City Developments Limited [2015] EWHC 1855 (TCC)

The facts

Caledonian Modular Limited ("Caledonian") and Mar City Developments Limited ("Mar) entered into a letter of intent in respect of extensive construction works in North London to which the Scheme for Construction Contracts 1998 ("the Scheme") applied in the absence of Construction Act compliant payment and adjudication terms.

Caledonian's first 14 applications for payment all followed the same format. They were accompanied by a letter attaching the detail of the interim application and setting out the total amount due, the amount previously certified and the net payment due. The letter also identified the date by which a payment notice was to be received, and the date for final payment. On 20 January 2015, Caledonian issued its application for payment number 15 ("Payment Application 15"), and on 5 February 2015, Mar issued what was agreed to be a valid payless notice which almost wiped out the sum claimed.

On 12 February 2015, Caledonian sent Mar an email relating to the ongoing negotiations for the final account. On 13 February, Caledonian emailed Mar an updated version of Payment Application 15 to reflect an agreement that had been reached between them in relation to one item, and asked Mar to update its payment notice to take account of the agreement, but Mar did not issue an updated payment notice as Caledonian had requested. Caledonian subsequently asserted that the updated payment application was a fresh payment application (number 16) and that Mar's failure to serve a payless notice in response to it rendered Mar liable for the full £1.5 million claimed. Caledonian's position was upheld by the adjudicator in the adjudication proceedings that followed, and Mar resisted enforcement by seeking a declaration as to the status of Caledonian's updated payment application.

The decision

Mr Justice Coulson held that the updated payment application did not constitute a new valid payment application under the Scheme, nor was it treated as such by the parties at the time it was issued. On 13 February 2015, Caledonian did not say, clearly or at all, that it was making a fresh application for an interim payment (even when challenged by Mar to explain what it amounted to). There was a fair inference that the updated payment application did not make clear it was a new application for interim payment because that was not how Caledonian itself viewed it; rather, it was an update of the final account. Moreover, the Judge emphasised that it was not possible for Caledonian to have served an updated payment application prior to the period for payment application 16 expiring; to do otherwise would make a mockery of the notice provisions under the Construction Act and the Scheme, and would run the risk of contractors making fresh claims every few days in the hope that, at some point, the employer or its agent would take their eye off the ball and fail to serve a valid payless notice.

Practice points

- When making an application for an interim payment or a payee's notice, you must set your claim out with clarity so that the employer is given reasonable notice that the payment period has been triggered. Ensure your application makes clear on its face that it is an application for an interim payment or payee's notice to avoid any later dispute as to its status.
- As Mr Justice Coulson held obiter in this case, interim applications probably cannot be made early, outside of the agreed payment mechanism, unless at the very least the fact that it is made early is drawn to the employer's attention. Given this was an obiter finding, you should err on the side of caution and always serve interim applications in strict accordance with the contractual payment dates.

Leeds City Council v Waco UK Limited [2015] EWHC 1400 (TCC)

The facts

Leeds City Council ("the Council") engaged Waco UK ("Waco") in relation to the design, manufacture and installation of modular classroom buildings at a primary school in Leeds under an amended JCT Design and Build Contract, 2005 Edition, Revision 2, 2009 ("the Contract").

The Contract included the usual interim payment provisions prior to practical completion on specific dates set out in the payment calendar that was included with the contract particulars. Waco's payment applications were issued roughly monthly, but never on the dates provided for by the Contract. As a general rule, the Council's agent and contract administrator ignored the fact that the payments were usually submitted a few days late, and the Council paid the amounts applied for.

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Following practical completion, the Contract provided that applications for interim payments were to be made at intervals of 3 months "unless otherwise agreed", and Waco continued to submit its payment applications erratically. The situation continued until 22 September 2014, when, post-completion, Waco made an application for payment, this time not late but 6 days early. The Council failed to serve a payment notice and did not pay the application, as a result of which Waco initiated adjudication proceedings and obtained an award for payment in its favour, but still the Council refused to make payment. Waco brought enforcement proceedings, and in response the Council sought a declaration that the adjudicator's decision was wrong on the basis that Waco's payment application of 22 September 2014 was invalid.

The decision

Mr Justice Edwards-Stuart found in favour of the Council and held that the contractual requirement for an application to be made on specific dates provided for by the Contract required Waco to state the total value of work that had properly been carried out as at the valuation date. Because Waco's payment application had been made 6 days before the valuation date, it was deemed by the court to be invalid.

Practice points

- When making payment applications, it may be possible for you to rely either upon an implied term, or an established course of dealing between the parties (for example, a series of payment applications made three or four days after the valuation date; a one-off payment would not suffice), which might allow you to submit the application within a reasonable time of the valuation date, but this would probably only stretch to a few days at the very most.
- It is important to note that there is no scope for payment applications to be submitted prior to the valuation date unless the contract makes express provision for the valuation dates to be varied (for example, by the use of the words "unless otherwise agreed").

Conclusion

The above decisions serve to confirm that it is imperative for parties to follow the contract to the letter in regard to payment and strictly observe all payment dates, or face what can be draconian consequences.

The position in regard to payment, however, is not entirely satisfactory. First, the decision in *Galliford Try v Estura* leaves a glaring loophole under the JCT suite which leaves it open to astute contractors to submit a very inflated payment application which is to all intents and purposes a final account.[5]

Secondly, the position in regard to interim payments and final accounts is inconsistent concerning compliance with notice provisions. For interim payments, there is a very strict approach to compliance, whereas in the case of final accounts the position is more indulgent. The Court of Appeal is due to revisit the position in regard to final accounts in November 2015 when it hears the appeal in *Harding v Paice*, and it therefore remains to be seen whether the more indulgent approach to final accounts will survive.

Footnotes

1. For full details of this case, see http://www.fenwickelliott.com/files/insight_issue_42.pdf.
2. For full details, see http://www.fenwickelliott.com/files/insight_issue_42.pdf.
3. In theory, it would have been possible for Estura to rectify its failure to serve a payless notice by issuing a payless notice at the next interim payment application, but by virtue of the fact that Galliford Try had recovered almost everything that it was hoping to recover in its interim payment application, it had no incentive whatsoever to submit its final account thus depriving Estura of challenging or reassessing the sum claimed in the interim application.
4. *Supra.*
5. The majority of JCT contracts do not provide for a repayment of any overpayment until the final account stage, even if a negative payment notice is issued. That said, some employers may seek to introduce an amendment providing for repayment of any overpayment prior to the final account stage and negative payments to counteract this.

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