ADJUDICATIO AND INSOLVENCY

Assignment and Rule 4.90
By Peter Sheridan

Introduction

A recent case has thrown up some new insolvency-related jurisdictional issues; in the process some perennial judicial concerns about adjudication have re-surfaced, including ambush and the suitability of adjudication for complex disputes. The case is also a rare example of the success of a "no dispute" jurisdictional argument. Coulson J's judgment is characteristically a model of clarity.

A Thames Water company known as Subterra was engaged by Thames Water Utilities to carryo out repair and maintenance works. Subterra engaged a sub-contractor, Tony McFadden Limited (TML) to carry out this work in the north London area. This sub-contract was known as the NLSDA sub-contract. Enterprise (the claimant in the case) then bought the business and assets owned by Subterra. The judge found that Subterra's sub-contract with TML was novated to Enterprise by way of the asset purchase agreement (and if it had not been, a novation by conduct could easily be inferred on the facts of the case). Enterprise then entered into three more sub-contracts with TML, so there were four sub-contracts between them in total.

TML then went into administration and then into liquidation.

The liquidators sent a detailed claim in respect of the NLSDA sub-contract to Enterprise but no response was made. The liquidators also sent a detailed claim on another of the sub-contracts, known as the Lot 8 sub-contract. Enterprise did respond on this occasion and notified its own claim, based on alleged overpayments of over £3 million.

The liquidators then assigned to Tony McFadden Utiilities Limited (Utilities) (the defendant in the case) what was called the "net EMSL balance", "EMSL" being the shorthand description of Enterprise, by deed of assignment. The "net EMSL balance" meant the balance due on the account arising out of the mutual dealings between TML and Enterprise, pursuant to rule 4.90 of the Insolvency Rules 1986.

Utilities purported to adjudicate against Enterprise over TML's disputed claim against Enterprise under the novated NLSDA sub-contract. Enterprise was the claimant in the court proceedings because it sought a series of declarations, contending for a variety of reasons that the adjudicator had no jurisdiction. The case came to court while the adjudication was still going on and Enterprise contended that it should be aborted forthwith.

The effect of the novation

As stated above, the judge found that there was a novation of the NLSDA sub-contract, so that the sub-contract between Subterra and TML became a sub-contract between Enterprise and TML. Enterprise could accordingly be

liable to TML for a claim made under the NLSDA sub-contract and the claim could be pursued in adjudication by TML. The judge stated that a novated construction contract in writing satisfies the requirements of section 107 of the Housing Grants, Construction and Regeneration Act 1996 (the HGCR Act).
These observations were peripheral to the case, which turned on the contractual link not between Enterprise and TML, but between Enterprise and Utilities, and on the deed of assignment.

The deed of assignment
Under rule 4.90 of the Insolvency Rules 1986, an account is taken of what is due from each party to the other in respect of their mutual dealings. Sums due from one party are set off against sums due from the other.
What was assigned to Utilities was the net balance arising out of the mutual dealings between Enterprise and TML, i.e. the net balance envisaged by rule 4.90 of the Insolvency Rules. The House of Lords had ruled in Stein v Blake that the claims each party has against the other are no longer capable of being assigned once there is a liquidation and rule 4.90 applies; all that is assignable is the amount due after the mandatory account is taken.
The commercial purpose of the assignment was that there would be a net balance in favour of TML and the entitlement to that balance would be assigned to Utilities. However, a purported assignment of the right to the positive balance only would be invalid. Coulson J found on the wording of the deed of assignment that it was not an invalid assignment of the right to the positive balance only, but a valid assignment following the mechanism explained in Stein v Blake of the right under rule 4.90.
The mutual dealings consisted of the four sub-contracts between Enterprise and TML.
The "net EMSL balance" was defined in the deed of assignment as the sum due upon the taking of accounts in respect of mutual dealings, "together with all rights appurtenany thereto including...the right to adjudicate..." Coulson J stated:

> "...it seems to me that, as a matter of law, an assignment of a right to adjudicate can be legitimate, although such a right needs to be attached to the underlying contract: see, in the context of arbitration, South v Chamberlayne."
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> Thus, if the deed of assignment in the present case operated as an assignment of TML's contractual claim against Enterprise under the NLSDA [sub-contract], then I consider that the right to adjudicate that claim will also have been validly assigned and there is no difficulty under section 107 of the [HGCR] Act."

In fact, for reasons explained further below, the judge did not find that the deed of assignment operated as an assignment of TML's contractual claim against Enterprise under the NLSDA sub-contract. The right to make a claim under the NLSDA sub-contract (or any of the other three sub-contracts) had not been assigned by TML to Utilities.

Could the rule 4.90 claim be adjudicated?
As a result of the assignment, Utilities, the assignee of TML, was entitled to

pursue its claim against Enterprise for an account and for the payment of what Utilities contended was the net balance due to it under rule 4.90. This was a claim that could not be pursued in adjudication, but would have to be pursued in court, as the judge found for the following reasons.

There were four sub-contracts; under the HGCR Act an adjudicator may only deal with one dispute under one contract. On the facts of this case, one of the sub-contracts was for van hire and was not a construction contract; an adjudicator would not have jurisdiction to consider it.

If, as in this case, the responding party has a cross-claim and considers that it would be entitled to the net balance from the claiming party (the assignees), then it would be necessary for them to join the assignors, in this case the liquidators of TML. The deed of assignment envisaged that course, but it could not happen in adjudication because it is not possible to have a tripartite adjudication.

In addition, rule 4.90 envisages that the account will be taken and the balance decided in one set of proceedings where the result will be final and binding. That would rule out adjudication, because the results could only be obtained piecemeal, contract by contract, and could only normally be temporarily binding.

The problems with the dispute purportedly referred to adjudication

Utilities did not seek to refer to adjudication the dispute as to its right to an account and a balance due under rule 4.90 (and could not properly have done so for the reasons given above). What Utilities did purport to refer, as stated above, was TML's disputed claim against Enterprise under the novated NLSDA sub-contract. There were several problems with this course.

First and fundamentally, the claim for sums due under the NLSDA sub-contract had "ceased to exist", in the unequivocal words of Lord Hoffmann in Stein v Blake. The only claim that could be assigned, as noted above, was the claim to a net balance. The claim under the NLSDA sub-contract could not be and was not assigned to Utilities; it was no longer extant and was incapable of assignment under the Law of Property Act 1925.

Secondly, the calculation of the net balance under rule 4.90 could not be performed in a piecemeal fashion, encompassed in multiple adjudications, particularly where not all the relevant parties could be joined in.

Thirdly, the judge perceived a fundamental clash between the certainty and finality envisaged by the rule 4.90 process and the temporary, quick-fix solution offered by adjudication under the HGCR Act. The judge pointed out that the Bouygues case (the only previous case that considered adjudication in the context of the Insolvency Rules) highlights the fundamental discrepancy between the rule 4.90 process for the balance of the account between the parties and the purported reference to adjudication of a dispute in respect of one element only of that balance, as part of a process that can in any event normally be opened up as of right.

It followed, of course, that the adjudicator in the adjudication that was still running did not have jurisdiction. However, Coulson J also had a second reason for concluding that the adjudicator did not have jurisdiction: the "no dispute" point referred to above.

The absence of a crystallised dispute

If there is no dispute, an adjudicator does not have jurisdiction. The point is often raised, but seldom succeeds because on the facts there generally is a dispute.

Here, Utilities took the assignment on 15 June 2009, but did not notify Enterprise of the existence of either the assignment or Utilities' claim as assignees for another three months. On 21 September 2009, Utilities gave notice of the assignment to Enterprise and on the very same day purported to refer the dispute under the NLSDA sub-contract to adjudication.

Coulson J found that in these circumstances the "no dispute" point arose with "stark clarity", because there was no possibility of a dispute between Utilities and Enterprise crystallising prior to the notice of adjudication. Utilities first gave notice of its claim at precisely the same time as referring the claim to adjudication. There was no interval between the two events. It is in this context that Coulson J refers to "ambush".

It was argued on behalf of Utilities that the dispute being referred was that which had crystallised between the liquidators of TML and Enterprise, Utilities was simply standing in the shoes of TML and was entitled to rely on the crystallisation of the original dispute. Coulson J held, however, that for a dispute to arise for the purposes of a reference to adjudication, there has to be a dispute between the two parties who are going to be the parties to the adjudication.

Prior to the case here under consideration, the "no dispute" argument has rarely succeed, but it has occasionally.

The course of the adjudication and complex disputes

Coulson J added a section to his judgment which expressed his views on the conduct of the adjudication, although these views were immaterial to his decision and were presumably not matters on which argument was heard or authority was cited. These remarks should be viewed with some caution, as what underlies them is, on analysis, judicial distaste for aspects of the HGCR Act which Parliament has enacted, which has been expressed by TCC judges on several occasions, as here, in the form of criticism of the parties or adjudicator where they have in truth been operating within that system.

Coulson J starts this section of his judgment with the opinion that the dispute was not, by reason of its sheer size, appropriate for the adjudication process. He made reference to the sum in dispute: a claim of £2.5m, for which it was necessary to understand the claim for the full account of £7 million; and to the volume of paperwork: 40 lever arch files, with a similar amount in Enterprise's response. Coulson J also referred to two judgments of Judge Toulmin CMG QC, the AWG and the CIB cases, which have been considered in some detail previously in Construction Act Review.

Coulson J stated that where the sheer volume/size of a claim may make it unmanageable in an adjudication, the course to be adopted by the adjudicator is clear. The adjudicator has to decide at the outset whether or not he can discharge his duty to reach a decision impartially and fairly within the time limit prescribed by the HGCR Act, as was stated in the CIB case. Coulson J

added that if he cannot, he ought to resign.

It is not clear at this point of the judgment if Coulson J is saying that an adjudicator should resign if in his judgment he cannot decide the dispute impartially and fairly within the 28-day or 42-day periods provided for in section 108 of the HGCR Act, or whether he means such period together with such extenstions of time as the parties agree. Coulson J is disparaging about the piecemeal extensions of time that occurred all the way through the adjudication, through to a date which made the period for the adjudication three times as long as the original period set down in the HGCR Act. This is in fact very similar to the approach taken by the adjudicator in the CIB case, the eminent QC John Uf. His approach, which included piecemeal extensions of time as he assessed the time needed to deal fairly with the issues, was described as "impeccable" by Judge Toulmin CMG QC. That too though was a large and complex final account claim with extensive documentation and this was apparent from the outset, so Mr Uff did not take the course Coulson J is saying the adjudicator in the present case should have taken.

When one reads in a TCC judgment some statistical analysis of large sums and numbers of files in the context of adjudication, it is often followed by some assertion to the effect that Parliament did not intend adjudication to be used for this type of complex dispute, Coulson J comes close to this:

> "Piecemeal extensions in large and paper-heavy final account disputes are not what the [HGCR] Act was designed for...this large final account claim was never suitable for adjudication."

The writer in fact agrees that this type of dispute is not suitable for adjudication and parties should not, in their own commercial interests, pursue this type of claim in adjudication. The writer does not agree that adjudication was not designed for it, in the sense that Parliament did not intend adjudication to be used for complex cases. On the contrary, it is quite clear on the plain wording of the statute that adjudication may be used for all disputes under construction contracts, however large and/or complex, as Judge Toulmin CMG QC was driven to accept in the CIB case. It is also the case that reference to Parliament's intention in this context is erroneous as there is no lack of clarity on this point that would justify invoking the Pepper v Hart rule and that, even if there were, it would be clear on examination that Parliament did intend adjudication to be available for all disputes. These points were explained in more detail in an earlier edition of Construction Act Review.

Further, the HGCR Act does specifically cater for piecemeal extension of time. Adjudications may be extended for as long as the parties agree; the agreement may be and frequently is made on a piecemeal basis. There is nothing in the statute to suggest that the agreement needs to be or should be made at the outset.

While in the writer's view Parliament's intention on these issues was not necessarily sensible, this is a criticism of the statute. However, it is not generally for judges to criticise legislation; commentators are not similarly constrained..

Coulson J was on firmer ground in encouraging adjudicators to give his non-binding view on jurisdictional objections, and in emphasising that an early

view on these points is helpful to the parties and can save costs.