

The Impact of Insolvency on Payment Entitlement

By Peter Sheridan

Normally a contractor is entitled to payment of certified sums and if there is no pay less notice from the employer, that right is easily enforceable in adjudication or in the courts. But the position becomes less straightforward if the contractor becomes insolvent before payment is made.

The position was considered by the House of Lords in *Melville Dundas Ltd v George Wimpey Ltd* (2007), before the Local Democracy, Economic Development and Construction Act 2009 (the LDED Act). It was held that that parties to a building contract could validly agree that, on termination, interim payments which had become due were no longer payable. The case was decided in respect of termination for insolvency, but the principle was not necessarily restricted to insolvency. The purpose of these termination provisions is to allow the employer to hold on to funds pending a final reckoning of claims and cross-claims, when a balance is due one way or the other.

The position was then dealt with in the statutory provisions of the Housing Grants, Construction and Regeneration Act 1996, as amended by the LDED Act (the HGCR Act). Under the HGCR Act s.111(1) the payer must pay the notified sum, but this is subject to s.111(10), which states that sub-section (1) does not apply where (a) the contract provides that, if the payee becomes insolvent the payer need not pay and (b) the payee has become insolvent. Therefore, the *Melville Dundas* approach was maintained by statute, but restricted to insolvency.

A case concerning two JCT Intermediate contracts, clause 8.7.3 of which provided that on the contractor's insolvency the employer "need not pay any sum that has already become due", recently came before the Court of Appeal (*Wilson and Sharp Investments Ltd v Harbour View Developments Ltd* (2015)). Clause 8.7.3 was part of the termination provisions of the contracts.

The contractor, Harbour View, had sums certified in its favour under both contracts. The employer did not issue pay less notices and did not dispute that the certified sums became payable. But it was common ground that the contracts were terminated (how and by which party did not have to be determined). The contractor entered into creditor's voluntary liquidation and was therefore insolvent as defined in the contracts; so the employer relied on clause 8.7.3. The trial judge's view that this clause did not apply where the relevant contract had already been terminated prior to the insolvency of the contractor was not accepted by the Court of Appeal, so the employer was correct that clause 8.7.3 was engaged.

Harbour View sought to present a winding up petition against the employer, on the basis that the employer was not paying debts that were due to be paid. However, such an application may be resisted if there is a bona fide dispute on substantial grounds. That was the position here, as it was arguable that the employer was not obliged to pay the sums due under the interim certificates but was entitled to delay payment until the taking of the final account under the termination provisions.

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The contractor was restrained by the Court of Appeal from presenting its winding-up petition. The employer argued that the works were over-valued in the certificates and that it had substantial claims against the contractor. These matters had to be bona fide and arguable on the facts for the employer to succeed.

It was also argued by the employer that it was the established practice in the Technology and Construction Court not to enforce interim payment obligations in favour of insolvent contractors. The Court of Appeal stated that the case law did establish that in appropriate circumstances, including where the contractor is insolvent, the court will refuse summary judgment (in the sense that a stay of execution is granted: see *e.g. Bouygues UK Ltd v Dahl-Jensen U K Ltd* (2000)). But it is not an absolute rule; the court looks at all the circumstances. It is important to establish not only that the contractor is insolvent but also that there is a genuine dispute over the contractor's claim to payment.

The *Bouygues* case (also in the Court of Appeal) had established that there might well be a compelling reason to refuse summary judgment arising out of an adjudication where there are cross-claims and one party is in liquidation.

Peter Sheridan

psheridan@sheridangold.co.uk