

Failure to Provide Collateral Warranty

By Peter Sheridan

It is normal under the terms of a construction contract for the contractor to be under an obligation to the employer to procure collateral warranties from its sub-contractors, and sub-consultants where the contractor has design and build obligations. The collateral warranties required are likely to be in favour of the employer and also other interested parties, such as a tenant or funder. The question may then arise as to what happens if the contractor does not provide the collateral warranties.

From the contractor's point of view, it should include in its sub-contracts provision which ensures that collateral warranties are provided at an early stage, for example making payment conditional on receipt of the warranties and making failure to provide the warranties a ground for termination of the contract.

An employer and other beneficiary of a warranty will also have an interest in seeing these types of provision in the sub-contracts. It is of course also essential for the employer/beneficiary to check that the obligation to provide the warranty has effectively been included in the sub-contract, so that the party providing the warranty has the obligation to the contractor to provide the warranty, just as the contractor has the obligation to the employer to procure it.

If the sub-contractor or sub-consultant has design responsibility, then it is important for the employer/beneficiary to check that the sub-contractor/ sub-consultant has professional indemnity insurance. Again, effective provision is needed that flows down into the sub-contract that not only requires the insurance to be in place but requires evidence of it to be supplied. Again, this should be linked to payment to ensure compliance. Frequently companies go into liquidation without having complied, by which time there is no effective remedy for the breach (not having the insurance).

If a contractor is obliged to but fails to procure a collateral warranty, an employer may apply to the court for an order for specific performance. This is a discretionary remedy whereby the court orders compliance with the obligation rather than damages for breach of it. It is therefore a remedy that is normally available only where damages would not be an adequate remedy.

This situation arose in *Liberty Mercian Ltd v Cuddy Civil Engineering Ltd* (2014). Damages against the contractor was not an adequate remedy, as it had no assets. Specific performance would offer an effective remedy and was ordered, as there was evidence that the party providing the warranty had professional indemnity insurance. The employer had terminated the contract with the contractor in this case, but the contractor still had the obligation to provide the warranty.

Specific performance will not be ordered if it serves no useful purpose. For example, in the *Liberty Mercian* case it would not have been ordered if the party providing the warranty were insolvent and not insured. Hence the importance of checking these matters at an early stage.

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