CONSTRUCTION ACT REVIEW

Insolvency and Adjudication: Liquidation

*By Peter Sheridan**

Introduction

This article is concerned with the legal considerations where a company in liquidation seeks to refer a dispute to adjudication. That involves a consideration of cases prior to the *Bresco* decision, the *Bresco* decision at first instance and in the Court of Appeal, the cases at first instance following *Bresco* in the Court of Appeal and finally *Bresco* in the Supreme Court, decided in June 2020.

The Insolvency Rules (IR) 2016 provide for the taking of an account of the parties' mutual dealings and arriving at a balance one way or the other under IR 14.25. In the pre-2016 cases, the applicable rule (with the same effect) was rule 4.90. This regime is referred to in this article as "insolvency set-off".

Bouygues[1]

Dahl-Jensen, a sub-contractor to Bouygues, obtained an adjudicator's decision in its favour which it sought to enforce. The adjudicator had made an error, the effect of which was to require Bouygues to pay the 5% retention to Dahl-Jensen, although it was not yet due under the sub-contract. The result of the adjudication was that over £200,000 was payable to Dahl-Jensen, whereas the correct position, taking into account the retention, was that sums were due to Bouygues. It was put to the adjudicator that he had made a slip, a contention he did not accept. The result at first instance was that the decision was enforced, because the adjudicator had decided the dispute referred to him; whether he had decided it correctly or not was nothing to the point.

While technically the enforcement was upheld in the Court of Appeal, a stay of execution was granted so that the monies did not change hands as envisaged at first instance, and the approach at first instance, to grant summary judgment in favour of Dahl-Jensen, was wrong and would not be followed again. The correct approach was set out in Chadwick LJ's judgment. At the date of the application for summary judgment and indeed at the date of the reference to adjudication, Dahl-Jensen was in liquidation. There were claims and cross-claims between the parties, which would be the subject of insolvency set-off. Chadwick LJ stated:

> "In circumstances such as the present, where there are latent claims and cross-claims between parties, one of which is in liquidation, it seems to me that there is a compelling reason to refuse summary judgment on a claim arising out of an adjudication which is, necessarily, provisional. All claims and cross-claims should be resolved in the liquidation, in which full account can be taken and a balance struck."[2]

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[1] *Bouygues UK Ltd v Dahl-Jensen UK Ltd* [2001] 1 All E.R. (Comm) 1041; [2000] B.L.R. 522; [2001] 3 T.C.L.R. 2; (2000) 73 Con. L.R. 135; [2000] C.I.L.L. 1673 CA.

[2] *Bouygues*, above, at [35].

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Enterprise Managed Services[3]

Thames Water entered into a contract with Subterra; Subterra entered into a sub-contract with TML. Enterprise bought Subterra's assets and there was a novation to Enterprise of the sub-contract with TML. There were also other sub-contracts between Enterprise and TML, so that there were four sub-contracts: the NLSDA sub-contract, the Lot 8 sub-contract, the Three Valleys sub-contract and a van hire sub-contract.

TML went into liquidation and the liquidators assigned assets to Utilities, which included contractual claims against Enterprise. Utilities then started an adjudication against Enterprise to pursue a claim under the NLSDA sub-contract. Enterprise sought declarations in connection with the adjudication.

Coulson J (as he then was) found that what was assigned to Utilities was the net balance arising out of the mutual dealings between Enterprise and TML. The right to adjudicate was also assigned; as a matter of law, an assignment of a right to adjudicate can be legitimate. However, it was the right to adjudicate a dispute as to an account of each party's claims and a payment of the net balance (required under the IR) that was assigned, not a right to adjudicate a dispute under the NLSDA sub-contract (or any of the other sub-contracts). These rights were caught by a prohibition on assignment;[4] the right to an account and payment of the net balance was not caught by the prohibition.

Coulson J went on to say that the net balance claim could not be pursued in adjudication, but would have to be pursued in court, for various reasons. Firstly, there were four contracts, whereas an adjudicator can deal with only one dispute under one contract, absent agreement. Secondly, the van hire agreement was not a construction contract and an adjudicator would have no jurisdiction to decide a dispute under it. Although not stated by Coulson J, this point again would be absent agreement to adjudicate the dispute. Thirdly, the responding party had cross-claims for which it would have to join the assignors, but adjudication is not a tripartite process. Fourthly, the Insolvency Rules envisage an account taken in one set of proceedings with a final and binding result. Adjudication would be piecemeal and only temporarily binding.

This fourth point does not survive the subsequent *Bresco* case, but the result would be the same today in the *Enterprise* case for the other three reasons.

In addition, by reference to the House of Lords decision in *Stein v Blake*,[5] on liquidation the only claim remaining was the net balance claim; the claim under an individual sub-contract had "*ceased to exist*". This over-simplifies the analysis in *Stein v Blake* as will be apparent when *Bresco* in the Supreme Court is considered below.

Coulson J also then referred to a "*fundamental clash*" between the Insolvency Rules and adjudication, a theme to which he returned and which he developed as a major consideration in the later Court of Appeal decision in *Bresco*, considered below. In the *Enterprise* case, he stated:

[3] *Enterprise Managed Services Ltd v Tony McFadden Utilities Ltd* [2009] EWHC 3222 (TCC); [2010] All E.R. (D) 126; [2010] B.L.R. 89; [2010] 26 Const. L.J. 204.
[4] These rights are not assignable anyway: see the Supreme Court decision in *Bresco*, discussed below.
[5] [1996] 1 A.C. 243.

> "…there is what I perceive to be a fundamental clash between the certainty and finality envisaged by the full rule 4.90 process and, to use the vernacular, the temporary, quick-fix solution offered by construction adjudication under the Act. How can a decision that, if challenged, is of a temporary nature only, and would relate just to one element of the chose in action, have any role or relevance to the taking of a final account under the Insolvency Rules?"[6]

> "In my judgment, *Bouygues* highlights the fundamental discrepancy between the pursuit of the only dispute that can now arise between the parties, namely, in respect of the balance of the account between them to be identified as part of the final and certain process under rule 4.90, and the purported reference to adjudication of a dispute in respect of one element only of that balance, pursuant to a process which can, in any event, be opened up as of right thereafter. This is a…reason why, in my judgment, Utilities have not sought to and cannot adjudicate their claim to the balance of the account arising out of the mutual dealings between the parties."[7]

Coulson J found for these reasons that the adjudicator in the purported adjudication concerning the NLSDA sub-contract did not have jurisdiction, although his view on this point was later rightly altered in *Bresco* in the Court of Appeal, considered below.

***Bresco* at first instance**

Bresco was a sub-sub-contractor to Lonsdale for the performance of electrical installation works. Bresco became insolvent and went into voluntary liquidation in 2015. In 2017, Lonsdale intimated a claim against Bresco, on the basis that Bresco's default led to the termination of the sub-sub-contract. Lonsdale's claim was for £325,541.92, principally made up of the cost of engaging a replacement sub-sub-contractor. In 2018, Bresco served an adjudication notice, purporting to refer a claim that Lonsdale had wrongfully repudiated the sub-sub-contract, together with claims for unpaid work and other sums amounting to about £220,000. Lonsdale asked the adjudicator to discontinue the adjudication on the basis that he had no jurisdiction; the adjudicator took the view that he did have jurisdiction.

Lonsdale obtained an injunction to prevent the continuation of an adjudication in which Bresco sought declarations and sums said to be due to Bresco. The basis for the injunction was Bresco's insolvency and Lonsdale's cross-claim.

Fraser J took the view, understandably on the authorities at the time, that the adjudicator did not have jurisdiction. In addition, since an adjudicator's decision in favour of a company in liquidation would not be enforced, the adjudication should not be permitted to continue. On this second point, Fraser J referred to *Philpott*[8] and to *Twintec v Volker-Fitzpatrick*.[9]

***Bresco* in the Court of Appeal**[10]

[6] *Enterprise Managed Services*, above, at [70].
[7] *Enterprise Managed Services*, above, at [72].
[8] *Philpott v Lycee Francais Charles de Gaulle School* [2015] EWHC 1065 (Ch).
[9] *Twintec Ltd v Volkerfitzpatrick Ltd* [2014] EWHC 10 (TCC).
[10] *Bresco Electrical Services Ltd (in liquidation) v Michael J Lonsdale (Electrical) Ltd & Cannon Corporate Ltd v Primus Build Ltd* [2019] EWCA Civ 27.

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There were two cases before the Court of Appeal, referred to here as "*Bresco*" and "*Cannon*". The *Cannon* case concerned a company voluntary arrangement (CVA) and will be considered in a separate article concerning adjudication and CVAs in a future edition of this journal. The *Cannon* case was already settled when the Court of Appeal gave its judgments and was not the subject of an appeal to the Supreme Court.

Coulson LJ stated:

> "The *Bresco* appeal raises directly the issue of whether an adjudicator can ever have the jurisdiction to deal with a claim by a company in insolvent liquidation. But there was also a related issue, concerned with whether (assuming that the adjudicator had the necessary jurisdiction) such an adjudication could ever have any utility and, if not, whether an injunction preventing the continuation of what would be a futile exercise was justified in any event."[11]

There were two arguments concerning jurisdiction. The first argument was that the right to refer any dispute to adjudication was lost when Bresco went into liquidation, because at this point there ceased to be any claim under the contract; it was replaced with the single right to claim the balance (if any), arising out of the mutual dealings and set-off between the parties. This argument was accepted by Fraser J at first instance.

On reviewing the leading decision, in the House of Lords in *Stein v Blake*[12] the *Bouygues* decision in the Court of Appeal and his own decision in *Enterprise Managed Services*,[13] Coulson LJ concluded that liquidation set-off does not, in principle, preclude the determination of the underlying claims. The proving of Bresco's claim was not a process extinguished by the occurrence of the liquidation. Lonsdale had conceded that Bresco's claim could have been brought in court or in arbitration, which went a long way towards accepting that it had not been extinguished. If it were not extinguished, the underlying claim therefore continued to exist, as Coulson LJ found, in a refinement of his view on *Stein v Blake*, expressed in the *Enterprise* case.

The only point then relied on (the second point concerning jurisdiction) was the temporarily binding nature of an adjudicator's decision. However, as a matter of jurisdiction, that factor did not mean that adjudication should be treated any differently from arbitration or court proceedings. Therefore, the adjudicator would have jurisdiction to consider a claim advanced by a company in liquidation and Coulson LJ stated that, in so far as he had suggested otherwise in the *Enterprise* case, he had been wrong to do so. The Court of Appeal therefore did not agree with Fraser J on the jurisdictional issue.

Coulson LJ then went on to Fraser J's other reason for granting the injunction, that the adjudication should not be permitted to continue as a matter of utility, the reasoning being that the adjudication would be futile.

Coulson LJ started by stating that he considered there is a basic incompatibility between adjudication and the regime set out in the IR 2016, the former being a method of obtaining an improved cash flow quickly and the latter an abstract accounting exercise, IR 14.25 envisaging the taking of a detailed account as between the company and the creditor and

[11] *Bresco*, above, at [3].
[12] *Stein v Blake* [1996] 1 A.C. 243.
[13] *Enterprise Managed Services Ltd v Tony McFadden Utilities Ltd* [2009] EWHC 3222 (TCC); [2010] All E.R. (D) 126; [2010] B.L.R. 89; [2010] 26 Const. L.J. 204.

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the careful calculation of a net balance one way or the other. The vast majority of claims in adjudication are not claims for a net balance of that type.

Coulson LJ re-stated the point made originally in *Bouygues* and which he had reiterated in the *Enterprise* case that an adjudicator's decision is only temporarily binding. While Coulson LJ had revised his view on this point in relation to jurisdiction, he still considered it directly relevant on the question of the utility of the adjudication. His point here was that a decision that is temporarily binding is not a condition or status envisaged by IR 14.25. This was therefore part of the basic incompatibility between adjudication and the insolvency set-off regime.

The result in cases where there is a cross-claim would be that the right to set off the cross-claim against the claim and thus to treat the sums claimed as security for the cross-claim would be lost if an adjudicator's decision on the claim were enforced. If Lonsdale had to prove its cross-claim in Bresco's liquidation, it would receive at best a dividend and would lose its right to liquidation set-off under IR 14.25.

Thus, the position was, as stated by Coulson LJ, that judgment in favour of a company in insolvent liquidation to enforce an adjudicator's decision, would only be granted in an exceptional case. Refusal of summary judgment or a stay will be the normal result. Coulson LJ also stated that a reference to adjudication of a claim by a contractor in insolvent liquidation, in circumstances where there is a cross-claim, would be incapable of enforcement and therefore an exercise in futility. This is the main point that was the subject of reversal in the Supreme Court.

Coulson LJ endorsed the solution to what he called the incompatibility problem adopted at first instance, the grant of an injunction to restrain the further continuation of the adjudication. He cited the first instance *Twintec* decision with approval as authority for the proposition that the court will grant such an injunction if the court concludes that the nascent adjudication is a futile exercise.

Meadowside[14]

In a well-reasoned judgment, Judge Constable subjected *Bresco* to a careful and detailed analysis. Meadowside, a building contractor engaged by the defendant (HSMC), was placed into voluntary winding up. Before that, practical completion was certified under the building contract. Before that, disputes had arisen.

Meadowside's liquidators appointed Pythagoras Capital Ltd (Pythagoras) to take over the pursuit of the sums Meadowside alleged were due to it under the building contract, by a funding agreement under which Pythagoras would receive a percentage of the recovery made. Pythagoras referred a claim to adjudication. HSMC raised jurisdictional objections, including that the claimant was in liquidation, and took no part in the adjudication. HSMC claimed to be a net creditor.

The adjudicator decided that he did have jurisdiction and found there was a net balance of £26,629.63 due to Meadowside. Before Pythagoras took steps to enforce, Fraser J decided at first instance in *Bresco* that an adjudicator did not have jurisdiction where the referring party was in insolvent liquidation. The Court of Appeal in *Bresco* then overturned the first

[14] *Meadowside Building Developments Ltd (in liquidation) v 12-18 Hill Street Management Company Ltd* [2019] EWHC 2651 (TCC).

instance decision that an adjudicator does not have jurisdiction in this situation, but the decision to grant injunctive relief to prevent the adjudication from continuing was upheld, on the ground of practical utility (futility).

The judge noted that *Bresco* left open the possibility that different considerations might apply if there were no cross-claim and left open the possibility that a company in insolvent liquidation may, in exceptional circumstances, succeed in adjudication, on enforcement and avoid a stay of execution.

In the *Enterprise* case, Coulson J had stated that it was not in accordance with the Insolvency Rules to calculate the net balance in a piecemeal fashion, absent agreement between the parties. Judge Constable pointed out that the parties' contract permitted adjudication at any time on any dispute; that might be thought to be such an agreement which does allow the piecemeal approach.

On futility, Judge Constable stated that, in considering the exercise of discretion, the usefulness of the adjudication, following liquidation, will be an important factor. The perception of usefulness will be shaped by the fact that the parties' substantive rights have been changed by the IR. In the *Meadowside* case, the adjudication was dealing with the full extent of the parties' mutual dealings, which made the factual position distinct from that in *Bresco* or *Enterprise*. The reason for this was that the adjudication dealt with the final account under the parties' construction contract. Although it was argued that it would be wrong to carve out a final account adjudication as an exception to the rule in *Bresco* and there was a risk of injustice with a final account adjudication, the judge stated this argument would tend to suggest there was no exception to the rule in *Bresco*, which is not what was stated in *Bresco*.

The judge also noted in relation to this argument that while there is de facto finality with an adjudication where a company is in liquidation instead of the usual potential temporary injustice, that would not be fatal to enforcement if safeguards could be put in place so as to maintain the temporary effect of the adjudication.

One aspect of the result in *Bresco* was that if a company in liquidation were entitled to a sum found in its favour by an adjudicator, and the responding party had a cross-claim, the responding party would be deprived of the benefit of treating the referring party's claim as security for its own cross-claim (set-off of mutual claims under the IR). Ordinarily, summary judgment is not available: see *Bouygues*. If the adjudicator's decision will not be enforced, the adjudication is an exercise in futility. Coulson LJ had quoted Judge Purle's observation in *Philpott* that it was "inconceivable" that an adjudicator's decision in favour of a company in liquidation would be enforced and said "this may put it too high", again indicating that the rule in *Bresco* was not absolute.

The judge then noted that if there were a satisfactory guarantee in relation to any sum ordered to be paid by the adjudicator and/or the sum were satisfactorily ring-fenced by the liquidator, the mischief at the heart of non-enforcement would be eliminated. He stated that even if there were no cross-claim, such security would be likely to be needed, so as to prevent the grant of a stay of execution on the usual application of the principles in the *Wimbledon* case.[15] So there could be an exception to the rule in *Bresco* where there are safeguards which meet the court's concerns.

[15] *Wimbledon Construction Co 2000 Ltd v Vago* [2005] EWHC 1086 (TCC); [2005] B.L.R. 374; 101 Con. L.R. 99. The case sets out well-known principles applicable to a stay of execution when summary judgment is granted to enforce an adjudicator's decision.

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The judge summarised where a case is likely to be an exception to the ordinary position as follows.

> "(1) The adjudication brought or to be brought determines the final net position between the parties under the relevant contract. An adjudication, by definition, will not be able to determine the net position between parties with dealings on more than one contract. The extent to which the adjudication is not capable of dealing with the entirety of the mutual dealings between the parties (and as such will not mirror the rule 14.25 process between the parties) is to be taken account of in all the circumstances when looking at the utility of the adjudication and the discretion either to injunct or, following adjudication, to enforce;
>
> (2) Satisfactory security is provided both:
>
> (a) in respect of any sum awarded in the adjudication and successfully enforced, so that it is repayable should the responding party successfully overturn the decision in litigation or arbitration brought within a reasonable time of the date of enforcement;
>
> (b) in respect of any adverse order for costs made against (or agreed by) the company in liquidation in favour of the responding party in respect of:
>
> (i) any unsuccessful application to enforce the adjudication decision;
>
> (ii) the subsequent litigation/arbitration, in which the responding party is seeking to overturn the adjudication decision.
>
> The extent to which any such costs order is ordered to be met from the security would be a matter for the court, insofar as it was not agreed.
>
> (3) What is satisfactory as security in form, duration and amount is a question on the facts in the ordinary way and may be provided incrementally (as it would be, for example, in any security for costs application). A combination of the following solutions might be appropriate:
>
> (a) the liquidator undertaking to the court to ring-fence the sum enforced so that it is not available for distribution for the relevant duration;
>
> (b) a third party providing a guarantee or bond;
>
> (c) ATE insurance." [16]

Although a letter by which Meadowside's liquidators appointed Pythagoras was disclosed, it did not set out the terms on which Pythagoras was to be paid, which must have been set out separately. The Damages Based Agreements Regulations 2013 permits a maximum recovery by the funder of 50% of sums awarded. The judge drew the inference that, although the percentage recovery agreed by Pythagoras was not disclosed, the percentage

[16] *Meadowside*, above, at [87].

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agreed was greater than the 50% permitted. The agreement was unenforceable, although this was primarily a matter between the liquidator and Pythagoras. However, it was also relevant to champerty; the agreement was contrary to public policy and champertous. While champerty does not of itself amount to an abuse of process, the establishment of champerty may be an element of abuse of process. The judge decided that, as a consequence of the refusal to disclose the terms of the funding agreement, the matter of abuse could not be satisfactorily disposed of and in these circumstances it would be wrong to grant summary judgment.

But for the issue of champerty, the judge would have allowed summary judgment, but issued a stay of execution. As the judge had stated, he saw no difficulty in the provision of a guarantee as part of a package of security seeking to meet the concerns expressed in *Bresco*. In this case, a guarantee from Pythagoras was offered. The judge did not consider Pythagoras to have adequate assets to stand as guarantor; a guarantee or bond should be from a bank or equivalent, providing a high degree of certainty that the guarantee will be called successfully. On that basis he would have granted the stay.

Balfour Beatty v Astec[17]

Astec was sub-contractor to Balfour Beatty under three sub-contracts dealing with aspects of work around Blackfriars station. Astec sought to bring three adjudications; Balfour Beatty applied for an injunction to restrain the adjudications. Astec had gone into liquidation, at which point both sides had claims or counterclaims against each other. By the time of the first adjudication, Astec had obtained funding from Pythagoras, which would be entitled to a significant, but not beyond 50%, fee from recoveries made by Astec.

Waksman J considered whether the case before him was one of the exceptional ones by reference to Judge Constable's analysis at paragraph 87 of the *Meadowside* judgment, quoted above, which sets out at sub-paragraphs (1) to (3) what Waksman J referred to as "the Meadowside Conditions".

In relation to the first of these, a single adjudication could not determine the final net position between the parties (absent agreement), because there were three contracts. However, three adjudications could do so, because there were no other mutual dealings between the parties and on the facts of this case the three adjudications would, when netted off against each other, arrive at a complete and comprehensive account of the parties' dealings. The judge held that that was satisfactory so far the first of the Meadowside Conditions was concerned.

In relation to security, Astec had to provide £250,000 for each contract as security for the costs of any subsequent litigation for a final determination of the matters decided in adjudication, subject to Balfour Beatty's right to apply for more if necessary. The judge also went through whether the terms of an insurance policy to cover these legal costs were satisfactory and the extent to which he required them to be altered. The judge allowed the adjudications to go ahead, but imposed conditions relating to the time at which the adjudications were started, required the parties to appoint the same adjudicator for each adjudication, and gave Balfour Beatty six months following the three decisions to bring legal proceedings, during which Astec could not enforce any adjudicator's decision.

[17] *Balfour Beatty Civil Engineering Ltd v Astec Projects Ltd (in Liquidation)* [2020] EWHC 796 (TCC).

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This case is accordingly an example of the exception to the rule in *Bresco*, as stated in the Court of Appeal following the analysis in *Meadowside*, in action.

Waksman J did address the question of the effect of the temporary nature of an adjudicator's decision on the enforceability of the adjudicator's decision, a point that may have been glossed over in *Meadowside*, stating:

> "And as for the point about adjudications only being temporarily binding, that cannot, in my view, survive *Bresco* because if it were correct, then as a matter of principle or jurisdiction, one could never have an adjudication in an insolvency situation. In truth, the points made by Coulson J here fade into the 'no jurisdiction' analysis which is now established to be wrong."[18]

In fact, this point did survive *Bresco* in the Court of Appeal, because Coulson LJ made it expressly clear that the temporariness of an adjudicator's decision was directly relevant to the incompatibility between the adjudication and insolvency set-off regimes, because the latter does not envisage a temporarily binding decision. However, the point does not survive *Bresco* in the Supreme Court, because the Court of Appeal was found to have been wrong on the incompatibility point.

***Bresco* in the Supreme Court[19]**

Bresco appealed against the order made by the Court of Appeal by way of an injunction restraining the pursuit of the adjudication. By cross-appeal, Lonsdale sought to restore the decision at first instance that the adjudicator lacked jurisdiction.

The Supreme Court found in Bresco's favour, both that the adjudicator had jurisdiction and that the Court of Appeal had been wrong to grant the injunction. Lord Briggs, with whom Lord Reed, Lord Kitchin, Lord Hamblen and Lord Leggatt agreed, made observations about the construction adjudication regime, that will no doubt be much quoted in adjudication cases, and then about insolvency set-off, before proceeding to analyse the position concerning jurisdiction and then futility and the incompatibility point.

The Construction Adjudication Regime

Lord Briggs started by describing adjudication as "a conspicuously successful addition to the range of dispute resolution mechanisms available for use in what used to be an over-adversarial, litigious environment."[20] He placed adjudication on a spectrum of dispute resolution mechanisms roughly between early neutral evaluation (ENE) and arbitration, stating:

> "Adjudication shares with ENE the independent, often expert, respected source together with the speed and economy of ENE, with a provisional element of binding

[18] *Astec*, above, at [15].
[19] *Bresco Electrical Services Ltd (in Liquidation) v Michael J Lonsdale (Electrical) Ltd* [2020] UKSC 25.
[20] *Bresco Electrical Services Ltd (in Liquidation) v Michael J Lonsdale (Electrical) Ltd* [2020] UKSC 25 at [10].

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> decision, unless and until the matter in dispute is later resolved by arbitration, by litigation or by agreement."[21]

In the course of general observations about the adjudication regime,[22] Lord Briggs noted that a very important underlying objective was the improvement of cash flow to fund ongoing works on construction projects, but that was not the sole objective of adjudication. Adjudication was designed to be and more importantly has proved to be a mainstream dispute resolution mechanism in its own right, which can be and is used to resolve final accounts and not merely interim payments. Adjudication in most cases also achieves a de facto final resolution because the adjudicator's decision is not challenged. There is no exclusion of particular types of legal person from the contractual right to require an adjudication, such as a company in liquidation, as there is in some comparable jurisdictions such as New South Wales.

Insolvency Set-Off

Lord Briggs noted that the legal and equitable rules of set-off do not encompass every type of cross-claim, in relation to current, contingent and future liabilities, but insolvency set-off operates on an altogether more comprehensive and rigorous basis. First, it applies to every type of pre-liquidation mutual dealing, and also to secured, contingent and future debts.[23] Secondly, whereas legal or equitable set-off is essentially optional, taking effect only if the cross-claim is pleaded as a defence to the claim, insolvency set-off is mandatory and takes effect upon the commencement of the insolvency (the 'cut-off' date). It is said to be self-executing, and for some purposes the original cross-claims are replaced by a single claim for the balance.[24] Thus, the separate cross-claims may no longer be assigned after the cut-off date: see *Stein v Blake*.[25] But the separate claims may survive for other purposes.[26] One example is the balance of contingent or prospective claims under IR 14.25(5).

Within the liquidation, a net balance owing to the creditor must be pursued by proof of debt in the ordinary way. The liquidator is entitled to be paid the full amount of any net balance owing by the other party claiming set-off, and may exercise any available remedies for its quantification and recovery, including litigation, arbitration or ADR: see IR 14.25(4) and (5).

If there is no dispute as to the existence and amount of the claims and cross-claims, the taking of an account is a matter of simple arithmetic. If any of the claims and cross-claims is in dispute, those disputes first need to be resolved before the arithmetic resumes.[27] Lord Briggs noted:

> "The process of proof of debt in the insolvency regime shares a number of the essential features of adjudication. Once initiated it is designed to operate both speedily and relatively cheaply. The liquidator is a professional likely to have some

[21] *Ibid.*
[22] *Bresco Electrical Services Ltd (in Liquidation) v Michael J Lonsdale (Electrical) Ltd* [2020] UKSC 25 at [10-26].
[23] IR 14.25(1), (2), (6) and (7).
[24] IR 14.25(3) and (4).
[25] [1996] A.C. 243.
[26] See *Wright v Eckhardt Marine GmbH* [2003] UKPC 37; [2004] 1A.C. 147 at [26-27] per Lord Hoffmann.
[27] *Stein v Blake*, above, per Lord Hoffmann at 255E-G.

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> experience or expertise in business of the type being conducted by the company, together with accounting expertise. The liquidator is also semi-independent. Although nominally asserting the company's position against the proving creditor, the liquidator is in substance adjudicating between the creditors as a whole in deciding what share of the available assets each should receive. The liquidator holds no brief for any particular creditor. The process of proof is (by comparison with litigation or arbitration) relatively light-touch and inquisitorial, and the outcome is only provisionally binding, in the sense that both the proving creditor and any other dissatisfied creditor may challenge the liquidator's ruling, by proceedings in court in which the issues are addressed de novo. It becomes final only if not challenged. In practice, as with adjudication, most of the liquidator's rulings in the process of proof are not challenged."[28]

The insolvency code is inherently flexible as to the best means of resolving disputes between the company in liquidation and third parties. There is no rule that merely because there exists set-off between cross-claims, and the need to take an account, disputes about all the claims and cross-claims need to be adjudicated upon in a single proceeding.

More generally liquidators are no strangers to ADR, or to the pursuit of the most cost-effective and proportionate means of resolution of disputes. The court has expressly approved the inclusion of third party determination procedures similar to adjudication in insolvency schemes of arrangement.[29]

Jurisdiction

It was common ground that the adjudicator would have had jurisdiction even though Bresco was in liquidation at the time of the adjudication, if Lonsdale had not had a cross-claim qualifying (if well founded) for insolvency set-off.

The main submission for Lonsdale was that because of the automatic operation of insolvency set-off all claims and cross-claims under the contract ceased to exist and were replaced by a single claim to the balance (by whichever party turned out to have the larger claim). This was not a claim under the contract but a claim under Bresco's insolvency.

One subordinate argument was that "a dispute arising under contract" has a narrower meaning in adjudication than in arbitration because it was imposed by statute. Lord Briggs was not persuaded that the statutory compulsion lying behind the conferral of the contractual right to adjudicate points at all towards giving the phrase "a dispute arising under contract" a narrow meaning, by comparison with a similar phrase in a contract freely negotiated. This is clearly correct; the writer has often observed in this journal that it is unlikely that parliament used the same expression in the HGCR Act as it used in the same year in the Arbitration Act with the intention of meaning something different.

Another subordinate argument was that even if disputes under the contract survived insolvency set-off, the requirement to resolve them all together in a single account could not be accommodated within an adjudication because of the "single dispute" rule in adjudication and the limited scope within adjudication for the determination of cross-claims.

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[28] *Bresco Electrical Services Ltd (in Liquidation) v Michael J Lonsdale (Electrical) Ltd* [2020] UKSC 25 at [32].

[29] See *In re Pan Atlantic Insurance Co Ltd* [2003] EWHC 1696 (Ch); [2003] 2 BCLC 678 at [32] per Lloyd J.

This argument, while accepted in the Court of Appeal, was considered in the Supreme Court to be misconceived. Firstly, there is no absolute "single dispute" rule in the HGCR Act or the Scheme. The only guidance in the Scheme is, in paragraph 8, that the adjudicator may determine more than one dispute, or disputes under more than one contract, if the parties so agree. Secondly, however narrowly the referring party chooses to confine the reference, a claim submitted to adjudication will nonetheless confer jurisdiction to determine everything which may be advanced against it by way of defence, and this will necessarily include every cross-claim which amounts to (or is pleaded as) a set-off. This was common ground but also supported by authority.[30] Thirdly, what is or is not a "single dispute" within the rule is by no means straightforward. Lord Briggs quoted the analysis of this issue by Akenhead J in *Witney Town Council v Beam Construction (Cheltenham) Ltd*[31] with approval. On this basis, a dispute about a cross-claim relied on as a set-off defence will be part of the dispute raised by the reference, because the claim cannot be considered without also considering the defence. Lord Briggs continued:

> "However, be that as it may, the single dispute rule would only assist Lonsdale's argument on jurisdiction if the law of insolvency set-off compelled the liquidator to bring all disputes about the claims and cross-claims qualifying for set-off for resolution in a single proceeding. But the law and practice of insolvency set-off does no such thing. The liquidator may, if it appears economical and proportionate to do so, untangle a complex web of disputed issues arising from mutual dealings between the company and a third party by picking some as suitable for adjudication, others for arbitration and others for disposal by an application to the court for directions, or by ordinary action. At the same time the liquidator may seek to deploy ADR and negotiation to narrow the issues in the meantime."[32]

The existence of a cross-claim operating by way of insolvency set-off does not mean that the underlying disputes simply melt away so as to render them incapable of adjudication. The submission that they are replaced by a dispute in the insolvency was wrong. If the argument were correct, if the company in liquidation had a disputed claim for £300,000 and there were an undisputed cross-claim for £25, this would trigger insolvency set-off and deprive the adjudicator of jurisdiction, which would be a "triumph of technicality over substance".[33]

The submission assumes, from an over-literal reading of the language of Lord Hoffmann's speech in *Stein v Blake*, that the claims and cross-claims which fall within insolvency set-off lose their separate identity for all purposes on the cut-off date. It is true that they do for the purpose of assignment, but there are important examples of purposes where they do not. Lord Hoffmann himself acknowledged this when he said that:

> "The cross-claims must obviously be considered separately for the purpose of ascertaining the balance. For that purpose they are treated as if they continued to exist."[34]

As noted above, a future or contingent claim may survive set-off so as to be enforceable as to the balance after the debt becomes due.

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[30] *PC Harrington Contractors Ltd v Multiplex Constructions (UK) Ltd* [2007] EWHC 2833 (TCC); [2008] BLR 16 at [40-41] per Clarke J. This principle was considered by the writer…
[31] [2011] BLR 707.
[32] *Bresco*, above, at [46].
[33] *Bresco*, above, at [48]. See also the further examples illustrating the argument is fallacious at [49].
[34] *Stein v Blake* at p 255E.

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Lord Briggs also agreed with Coulson J in the Court of Appeal that if, as was common ground, a liquidator was entitled to pursue its claims by arbitration, the same applies to the right to refer disputes to adjudication.

Futility

Lord Briggs stated that once it is appreciated that there is jurisdiction, the insolvent company has both a statutory and a contractual right to pursue adjudication. It follows that it would ordinarily be entirely inappropriate for the court to interfere with the exercise of that statutory and contractual right. Injunctive relief may restrain a threatened breach of contract but not, save very exceptionally, an attempt to enforce a contractual right, still less a statutory right.

As already explained, it was simply wrong to suggest that the only purpose of construction adjudication is to enable a party to obtain summary enforcement of a right to interim payment for the protection of its cash flow, although that is one important purpose.

Adjudication is a beneficial means of dispute resolution that is not incompatible with the insolvency process, still less an exercise in futility.

> "First, as already described, the process of proof of debt in insolvency shares many of the attractive feature of adjudication, in terms of speed, simplicity, proportionality and economy, but adjudication has the added advantage that a construction dispute arising during an insolvency will be more amenable to resolution by a professional construction expert than by many liquidators."[35]

Lord Briggs continued to state that:

> "It is true that the effect of insolvency set-off may mean that cross-claims raise issues wholly outwith the purview of one or more construction contracts…In such a case the adjudicator will need to have regard to them, if they amount to a defence to the disputed construction claim being referred, but may have simply to make a declaration as to the value of the claim, leaving the unrelated cross-claim to be resolved by some other means. That is a remedy well within the adjudicator's powers. Nonetheless the adjudicator's resolution of the construction dispute referred by the liquidator may be of real utility to the conduct of the process of set-off within the insolvency process as a whole."[36]

Thus an adjudicator will need to consider if there is any cross-claim from the responding party in the adjudication that is a defence to the claim made in the adjudication by way of set-off. If so, the adjudicator will have to decide on both the claim and the set-off; that is the position in any adjudication, regardless of whether the claimant is in liquidation. If the responding party has a cross-claim that is not a defence to the claim made in the adjudication by way of set-off, then it would seem that, if the adjudicator is aware of the cross-claim, the adjudicator may have to limit the relief granted to declaratory relief rather than an order for payment. A cross-claim that is not a defence to the claim made in the adjudication may arise in a number of ways. For example, the responding party may have a claim under another contract, and the contract which is the subject of the adjudication may

[35] *Bresco*, above, at [61].
[36] *Bresco*, above, at [63].

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not contain provision permitting legal set-off between one contract and another. Or the responding party may have a claim under the contract which is the subject of the adjudication, but is unable to run it as a defence of set-off because it has failed to serve a valid pay less notice. The cross-claim in these situations still remains to be dealt with as a matter of insolvency set-off; the Supreme Court's guidance here is that declaratory relief may be the appropriate route for the claim made in the adjudication and is likely to be useful in providing information as to one element of the insolvency set-off. Of course, quantum may be relevant here; if the cross-claim is not claimed to extinguish or overtop the claim, then an order for payment of some of the claim may still be appropriate.

Lord Briggs took the view that there was no need for an injunction in *Bresco*; as the adjudication was a potentially useful means of ADR in its own right, there was no benefit in preventing the adjudication running its speedy course. The court is well placed to deal with the separate question whether the adjudicator's decision should be enforced, as explained in *Bouygues*.

In some cases, enforcement will be appropriate, for example if there is no dispute about the cross-claim and the claim is found to be in a larger amount. Or the disputed cross-claim may be found to be of no substance. Or, if the cross-claim can be determined by the adjudicator because the claim and cross-claim form part of the same dispute under the contract, the adjudicator may be able to determine the net balance.

It is true that an adjudicator may over-value the net balance in favour of the company in liquidation, so that summary enforcement leaves the respondent having first to establish a true balance in its favour and then pursue it by proof against an under-funded liquidation estate. But that may occur in any liquidation context.

Lord Briggs stated that:

> "The proper answer to all these issues about enforcement is that they can be dealt with…at the enforcement stage, if there is one. In many cases the liquidator will not seek to enforce the adjudicator's decision summarily. In others the liquidator may offer appropriate undertakings such as to ring-fence any enforcement proceeds: see the discussion of undertakings in the *Meadowside* case. Where there remains a real risk that the summary enforcement of an adjudication decision will deprive the respondent of its right to have recourse to the company's claim as security (pro tanto) for its cross-claim, then the court will be astute to refuse summary judgment."

Coulson LJ had made further points about the responding party having to incur wasted costs and the burden on the courts in relation to the futility argument. As for costs, Lord Briggs pointed out that parliament chose to make adjudication costs neutral. Many forms of ADR are costs neutral and none the worse for that. So also, in the insolvency context, is the process of proof of debt. Lonsdale argued that that a joint and several liability to pay the adjudicator's fees may leave the respondent having to pay the whole amount with no effective recourse. However, that liability of the company will be a liquidation expense, rather than a matter of proof and although that may not be a complete guarantee of payment, it provides reasonable reassurance and a joint and several liability of this kind is not generally risk free.

As for the burden on the court, this consideration militates against, rather than in favour of, admitting applications for injunctions to restrain adjudications before they have run their course.

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Conclusions

It should be borne in mind that *Bresco* is primarily about jurisdiction and whether an injunction should be granted to restrain the continuation of an adjudication; it is therefore of narrow scope. On these narrow points, the position is now clear and simple. A party in liquidation may pursue a claim in adjudication. The adjudicator does not lack jurisdiction by reason of the fact that the referring party is in liquidation nor by reason of a combination of the referring party being in liquidation and the responding party having a cross-claim or cross-claims. The adjudicator should accordingly proceed to decide the matters referred. A responding party will not now succeed in seeking an injunction to restrain the continuation of the adjudication, by reason of the fact that the referring party is in liquidation nor by reason of a combination of the referring party being in liquidation and the responding party having a cross-claim or cross-claims.

Although it is not a case about enforcement, the Supreme Court decision in *Bresco* does offer some guidance on the enforcement position. Some earlier cases bearing on enforcement remain important and for that reason were considered above. *Bouygues* was not criticized or doubted by the Supreme Court in *Bresco*. It remains the position that if the *Bouygues* facts or similar came before the court, summary judgment would be refused, because it would have been wrong for Dahl-Jensen to be paid the sum ordered by the adjudicator when on a proper analysis of insolvency set-off sums were likely to be due to Bouygues.

Bouygues does not lay down a general principle that an adjudicator's decision in favour of a company in liquidation can never be enforced, nor that an adjudicator's decision in favour of a company in liquidation can never be enforced if there is a cross-claim. The circumstances, including the quantum and merit of the claim and cross-claim have to be considered, as they were in *Bouygues*, where the facts happened to be simple and stark.

The *Meadowside* case remains significant, although it is no longer necessary to find a way round the futility argument, which has now been rejected by the Supreme Court. However, *Meadowside* is still important with regard to the route by which a liquidator may achieve enforcement of an adjudicator's decision in favour of the company in liquidation, by providing satisfactory security as set out above.

Balfour Beatty v Astec was concerned with an injunction, a situation that will not arise post the Supreme Court decision in *Bresco*, but the consideration of "the Meadowside Conditions" in *Balfour Beatty v Astec* remains relevant to enforcement cases.

As noted in *Meadowside*, an adjudicator's decision which determines all the parties' claims and cross-claims will thereby carry out the insolvency set-off exercise. This may occur for example where the only contract between the parties is a construction contract and the adjudicator decides the final account or the net balance due following a termination under that contract. A decision of this type is likely to be enforced, if the concerns over preserving the temporariness of the decision are met by the types of measures as to security discussed in *Meadowside* and *Balfour Beatty v Astec*.