HFW

CONSTRUCTION BULLETIN
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Welcome to the September 2020 edition of our Construction Bulletin.

In this edition we cover a broad range of recent developments in international construction law, as follows:

- The Future Is Virtual - Why Virtual Hearings Should Become the Go-to Platform for Adjudications, Arbitrations and Short Hearings
- Back-to-back Payment Provisions in the UAE – Are They Always Enforceable?
- Merits Review: New Australian Case Concerning the Court's Ability to Review Adjudicators' Decisions
- Insolvent Companies Can Pursue Adjudication - Bresco

The inside back page of this bulletin contains a listing of the events at which the members of the construction team will be speaking over the upcoming months.

Michael Sergeant, Partner michael.sergeant@hfw.com
Joanne Button, Associate joanne.button@hfw.com

CHRIS PHILPOT
SENIOR ASSOCIATE, LONDON

"Virtual hearings should become the go-to platform for adjudications, arbitrations and short hearings."

THE FUTURE IS VIRTUAL

We recently acted for the claimant in a major infrastructure dispute valued in excess of €140million. The claim involved a highly complicated multi-faceted dispute including delay, variations and unforeseeable ground conditions. There were multiple pleadings with over 5000 document pages.

The two week hearing took place virtually over Microsoft Teams. Oral evidence was heard from thirteen witnesses and ten experts on a range of areas and specialisms, interspersed with submissions from legal representatives.

This article outlines why virtual hearings should become the go-to platform for adjudications, arbitrations and short hearings.

Attendance

The dispute involved companies based in different countries, with legal representatives and experts based around the globe. A key practical benefit was that legal representatives, witnesses and experts did not have to travel to a designated venue each day. Attendees simply logged on from wherever in the world they were. This eliminated flight and accommodation costs, avoided non-productive travel time and removed all venue costs.

The Hearing

A virtual hearing always starts on time. There was also the flexibility to sit later or start earlier. Whilst the hearing took place over 2 weeks, 'rest' days were incorporated into the schedule, which is not usually practical with a traditional "in person" hearing and a hired venue.

A key benefit to virtual hearings is the use of electronic bundles, which facilitated a smoother hearing. Despite there being a considerable number of documents referred to, no time was lost searching for a paper document. Instead, witnesses and experts were instantly presented with the relevant excerpt of a document displayed on the screen, visible to all through screen-sharing. This meant everyone at the hearing was immediately focused on the same document, at the same time, with no distractions.

The virtual hearing also provided a far better forum for presenting photographs, videos and explaining complicated aspects of a case through graphics and diagrams. We used spreadsheets, charts and slides and were able to highlight and annotate these in real time to emphasis a particular point. When cross-examining witnesses, we used interactive maps, surveys and videos to explain issues and help raise questions. The virtual platform facilitated the easy use of technology in this way, which is otherwise cumbersome. It also made it much easier to present witnesses with documents in cross-examination which were not already in the bundle.

When giving evidence, witnesses and experts sat close to their webcam meaning body language and non-verbal cues could be observed as easily as if attendees were in the same room.

Conclusion

Virtual hearings facilitate the use of different technologies to present evidence in formats not ordinarily accessible in a non-virtual hearing. Virtual hearings save considerable costs, eliminate travel time, reduce demands on witnesses and allow greater flexibility in the hearing process itself.

At the conclusion of the Hearing, there was consensus among the parties that there was a key future role for virtual hearings after Covid-19. The upside to virtual hearings are so significant that, in our opinion, they are possibly the future for all adjudications and arbitrations.

CHRIS PHILPOT
Senior Associate, London
T +44 (0)20 7264 8336
E chris.philpot@hfw.com

BACK-TO-BACK PAYMENT PROVISIONS IN THE UAE – ARE THEY ALWAYS ENFORCEABLE?

It is common to find "pay-when-paid" or "pay-if-paid" provisions in construction subcontracts in the UAE. Such back-to-back payment provisions act as a risk-sharing agreement between the parties, whereby the subcontractor agrees to defer its entitlement to payment until the contractor receives such monies from the employer.

However, there are some circumstances in which back-to-back payment provisions may be deemed unenforceable under UAE law.

1. When non-payment by the employer is due to contractor breach, with no default by the subcontractor, a tribunal may uphold the subcontractor's claim, as it is contractor default that precludes payment, not subcontractor breach. Article 894 of the UAE Civil Code (which deals with prevention to completion of the works) and legal principles relating to good faith and unlawful exercise of rights provide the legal support for claims arising out of such circumstances.
2. In Case No. 281/95, Dubai Court of Cassation held that, despite the existence of a back-to-back payment clause, there was no justification for making a subcontractor wait for payment once a project has been completed and handed over to the employer.
3. Article 428 of the UAE Civil Code provides that a condition must be observed as far as possible. Therefore, a tribunal may require evidence of continued pursuit of legal proceedings by the contractor, to support its defence that adequate steps have been taken to pursue the subcontractor's payment.
4. A tribunal may deem that, under the UAE Civil Code, cancellation of the project results in cancellation of the subject matter of the contract, including cancellation of the subcontract, in which case the tribunal is likely to order restitution of monies due under the subcontract.
5. Dubai Court of Cassation case 303/2013 held that the pay-when-paid clause in that case was waived when the contractor paid part of the monies claimed by the subcontractor, despite maintaining that such monies had not been received from the employer.
6. Another reason for the failure of the pay-when-paid clause in case 303/2013 was that the contractor was unable to demonstrate that monies received from the employer did not relate to the subcontractor's works, leading to an inference of fraud, which the Court also indicated would nullify the pay-when-paid clause.
7. In Cassation No. 151 of 2014, Abu Dhabi Court of Cassation rejected the back-to-back defence in circumstances where it became impossible for a contractor to receive payment from the employer.

The Court confirmed the general principle that the contractor's receipt of payment is a pre-requisite for the subcontractor to claim its payment under a back-to-back clause.

However, the Court also held that, under Articles 472, 893 and 894 of the UAE Civil Code, such obligation shall be terminated if it becomes impossible to perform.

Therefore, where the project works were suspended and the subcontract agreement could not be performed due to reasons beyond the contractor and the subcontractor's control, the subcontractor was legally entitled to claim outstanding amounts due under the subcontract.

MARIA DEUS
Legal Director, Abu Dhabi
T +971 2 235 4907
E maria.deus@hfw.com

MARIA DEUS
LEGAL DIRECTOR, ABU DHABI

"Back-to-back payment provisions act as a risk-sharing agreement between the parties."

JAMES THYER
ASSOCIATE, MELBOURNE

"Ultimately, it is for any party seeking to adopt a "different procedure" to make such an application. Absent compelling reasons to deviate from the "general procedure", it is difficult to see how any litigant could convince a court to drive the proverbial B-double through SOPA."

THE MERITS REVIEW IS DEAD, LONG LIVE THE MERITS REVIEW

In a recent judgment, the Supreme Court of Victoria in Australia considered the extent to which a court, in exercising its supervisory powers in an application for judicial review, should delve into the merits in order to determine whether an adjudicator's decision under the *Building and Construction Industry Security of Payment Act 2002* (Vic) (SOPA) should be overturned.

SOPA

SOPA establishes a statutory adjudication system designed to ensure that building industry participants are provided with means to rapidly progress disputes concerning entitlement to payment. Often referred to as a 'pay now argue later' regime, the statutory adjudication process results in a prompt, interim determination of amounts payable to a downstream party.

An adjudicator undertaking the statutory determination functions has been held to be a tribunal exercising governmental powers or functions of a public nature because they exercise *"statutory power in a quasi-judicial capacity"*,[1] and as such their decisions are subject to judicial review.

Judicial review has traditionally been seen as involving a direct review by the superior court of the legality of an administrative decision, as part of the court's supervisory jurisdiction.

In Victoria, a party seeking review of an adjudication determination must demonstrate either jurisdictional error, or, error of law on the face of the record.

The case

In *Watpac Constructions Pty Ltd v Collins & Graham Mechanical Pty Ltd*[2], the Victorian Supreme Court refused an application for judicial review of an adjudicator's determination.

Collins & Graham Mechanical Pty Ltd (CGM) entered into a contract with Watpac Constructions Pty Ltd (Watpac), for CGM to perform the mechanical services package on a hospital expansion for which Watpac was the head contractor.

Following a series of adjudication determinations in favour of CGM, Watpac issued a notice purporting to take the remaining work under the contract out of CGM's hands (Take Out Notice). CGM contended that the Take Out Notice was repudiatory, accepted the repudiation and elected to terminate the contract.

CGM thereafter issued a payment claim under SOPA. Watpac issued a payment schedule in response, disputing the validity of the payment claim and certifying a large sum in favour of Watpac. CGM proceeded with an adjudication application which was substantially successful with the adjudicator determining that a sum was payable to CGM.

Watpac was aggrieved by the adjudicator's determination and applied to set aside the determination.

Central issues

A key concept of SOPA is the notion of a 'reference date' (the date from which a payment claim can be made). The existence of a reference date is determined either by the contract, or if it does not expressly provide, the default provisions in SOPA.

In the adjudication, CGM relied upon a clause in the contract which, it said, provided a reference date for the making of the claim under consideration. The relevant clause only provided a reference date if the conduct of Watpac in issuing the Take Out Notice was repudiatory, and CGM had elected to terminate the contract.

Watpac unsurprisingly contended that the Take Out Notice was valid and no reference date accrued.

The adjudicator determined that the Take Out Notice was invalid, a reference date had accrued, and CGM's claim was valid.

Watpac's application for review challenged the adjudicator's findings in respect of these matters.

The judicial review proceedings before the court essentially turned on two issues, first the validity of the Take Out Notice, and second whether the terms of the contract provided a reference date for the making of a claim for payment if the Take Out Notice was invalid.

The first issue is a question of fact whereas the second is a question of law, but each could notionally give rise to a *"jurisdictional fact"*. This distinction could fundamentally alter how a court exercises its supervisory power on review.

Process on judicial review

The typical procedure in a review application is quite different to a trial at first instance.

So far as questions of law are concerned the process is identical. A court will decide which statement of the law is correct having heard the submissions of the parties.

Questions of fact in a review application are typically determined on the basis of evidence set out in affidavits filed by the parties. The evidence is not typically tested through the prism of cross-examination and this is where difficulties can arise, especially when a determination as to disputed facts is necessary to establish (or otherwise) a *"jurisdictional fact"*.

This was precisely the issue the court had to grapple with here. Each party contended that it had validly ended the contract premised on either a repudiation of the contract by Watpac, in the case of CGM, or the issue of valid Take Out Notice, in the case of Watpac.

In order to properly and finally determine which party was right about termination of the contract and thus determine the existence or otherwise of a reference date, being a critical jurisdictional fact, a Court would adopt ordinary trial procedure.

The parties would exchange pleadings, evidence would be received in admissible form and tested through the rigour of cross-examination. The problem with this process in the context of proceedings involving SOPA was highlighted by the learned Judge.[3]

The learned Judge held that the *"adoption of such a process 'would drive a horse and cart (or perhaps a B-double) through the legislative scheme, and neither party sought to do so. If a party does not apply to conduct a fully blown trial in a future application under this Act, it may be necessary for the Court to consider whether, in exercising its residuary discretion in a judicial review proceeding, it should refuse such an application."*[4]

In making this statement, the court was mindful of the intent of the statutory adjudication scheme which includes securing prompt entitlements to payment and highlights the traditional policy that a court will be reluctant to adopt procedures in a judicial review application that would be inimical to its function.

Somewhat surprisingly there appear to be no other cases that have squarely considered this issue and the processes to be adopted in the context of SOPA.

Looking to other jurisdictions, the courts in the UK are much more averse to opening up an adjudication decision. Generally speaking, courts in the UK enforce adjudication decisions readily, and will not consider factual disputes or incorrect applications of the law when doing so. The UK courts will only intervene in the enforcement of an adjudication decision if it is found that the adjudicator did not have jurisdiction or if there was a breach of the rules of natural justice.

In this matter, where neither party pressed the court for a full hearing on the issue of termination, the court found that Watpac (being the aggrieved party) had failed to discharge its onus in establishing the non-existence of the *"jurisdictional fact"*.

Potential for a new process in some instances?

His Honour did however leave open whether questions of fact could be susceptible to judicial review.

The learned judge did not reject the concept that a *"different procedure"* could be adopted in order to test a question of fact, but opted to state that if the court were to consider a *"different procedure"*, this would call into question the extent to which it would be exercising its supervisory powers on judicial review or acting as a trial court with respect to specific factual matters.

It is difficult to envisage cases where the benefits of the court finally determining the existence of specific facts would outweigh the violence done to the objects of SOPA, especially the object of securing prompt payment.

However, if the court were to do so it is suggested the relevant factors may include: the commercial position of the relevant parties (relevant to the importance of preserving cashflow and the objects of SOPA); the scope of the factual inquiry (relevant to the time and resources needed to resolve the disputed question of fact); and whether the disputed questions of fact would resolve, or assist in resolving, disputes between the parties (relevant to the utility of a trial process).

Ultimately, it is for any party seeking to adopt a *"different procedure"* to make such an application. Absent compelling reasons to deviate from the *"general procedure"*, it is difficult to see how any litigant could convince a court to drive the proverbial B-double through SOPA.

JAMES THYER
Associate, Melbourne
T +61 (0)3 8601 4534
E james.thyer@hfw.com

1 *Grocon Constructors Pty Ltd v Planit Cocciardi Joint Venture (No 2)*, [2009] VSC 426, [79].

2 [2020] VSC 414.

3 at [43].

4 at [44].

STEPHANIE YU
SENIOR ASSOCIATE, HONG KONG

"In the midst of Covid-19 and economic downturn, it remains to be seen whether more insolvent companies in the construction industry will opt for adjudication as provided under the contract or by statute."

INSOLVENT COMPANIES CAN PURSUE ADJUDICATION: BRESCO[1]

The UK Supreme Court considered the conflict between the adjudication regime[2] and the automatic operation of insolvency set-off[3] and their incompatibility in *Bresco*, and confirmed that they were *not* incompatible despite the existence of cross-claims.

There have been numerous updates on this important decision, but very few have considered the potential extra-territorial impact in jurisdictions without statutory adjudication, such as Hong Kong. Bresco remains relevant because it is not uncommon for construction contracts to provide for adjudication. For instance, with the rise in the use of NEC standard forms as mandated by the Hong Kong Government.

Background

In 2014, Bresco undertook to perform electrical installation work for Lonsdale. In 2015, Bresco went into liquidation. Both parties claimed they were money owed by the other.

Bresco's liquidators referred the claim to adjudication. Lonsdale objected, claiming there was no dispute under the contract (due to insolvency set-off), and the adjudicator lacked jurisdiction to hear the dispute (jurisdiction point). Lonsdale also claimed that even if there was jurisdiction, adjudication was pointless since the adjudicator's decision is unenforceable until the net balance is calculated (futility point).

Fraser J granted an injunction to stop the adjudication. On appeal, Bresco succeeded on the jurisdiction point but the injunction was upheld due to the futility point. Bresco appealed to the Supreme Court and Lonsdale cross-appealed.

Decision

The Supreme Court allowed the appeal and dismissed Lonsdale's cross-appeal because: (1) the existence of cross-claims operating by way of insolvency set-off does not mean that there is no dispute under the contract, or that the claims have *"... melted away so as to render them incapable of adjudication."* Claims arising under the contract should continue to be treated separately to the claim for insolvency set-off; (2) if a liquidator was entitled to pursue the company's claims by arbitration then the same must apply to adjudication. There is no reason to treat the two differently; (3) the insolvent company has both statutory and contractual right to pursue adjudication and *"it would be... inappropriate for the court to interfere with the exercise of that statutory and contractual right"*; and (4) resolving cash-flow issues should not be the only objective of adjudication which was designed to be a *"mainstream dispute resolution mechanism in its own right..."*.

Lessons Learned

- Adjudication, on the application of the liquidator is **not** incompatible with the insolvency process. The adjudicator **has** jurisdiction.
- It is **not** an exercise of futility merely because there are cross-claims within insolvency set-off.
- The courts may be reluctant to restrain insolvent companies from proceeding with adjudication.

Conclusion

In the midst of Covid-19 and economic downturn, it remains to be seen whether more insolvent companies in the construction industry will opt for adjudication as provided under the contract or by statute. The UK Supreme Court has highlighted the benefits of adjudication in providing a speedy, cost effective and final resolution of disputes.

Whilst insolvency set-off is applicable in Hong Kong, statutory adjudication has not been formally introduced[4], but if adjudication is provided for in a contract, parties should keep the lessons learned from *Bresco* in mind.

STEPHANIE YU
Senior Associate, Hong Kong
T +852 3983 7658
E stephanie.yu@hfw.com

1 *Bresco Electrical Services Ltd (In Liquidation) (Appellant/Cross-Respondent) v Michael J Lonsdale (Electrical) Ltd (Respondent/Cross-Appellant)* [2020] UKSC 25

2 Under section 108 of the Housing Grants, Construction and Regeneration Act 1996 and also the contractual provision for adjudication in the underlying contract

3 Under rule 14.25 of the Insolvency (England and Wales) Rules 2016

4 Hong Kong is currently formulating legislation on security of payment, which includes adjudication. A consultation paper was issued in June 2015 and a report was released in April 2016.

LIST OF UPCOMING EVENTS

Construction Law Virtual Summer School
Workshop: Variations under the FIDIC Contracts
8 September 2020 (11.55am BST)
Speaker: Michael Sergeant

Construction Law Virtual Summer School
EPC Contracts
8 September 2020 (2.10pm BST)
Speaker: Ben Mellors

Offshore Decommissioning Virtual Congress
Contracting Strategies for Offshore Wind Decommissioning
16 September 2020 (10.30 BST)
Speaker: Richard Booth

HFW Offshore Wind Webinar Autumn Series
Practical insights into the use of FIDIC (2017) in Offshore Wind Projects
22 September 2020 (9am - 10am BST)
Speakers: Max Wieliczko, Michael Sergeant, Richard Booth

The Chartered Institute of Building MENA Webinar
Variations in Construction Projects
23 Sept 2020 (4pm - 5.30 pm BST / 7pm – 8.30pm GST)
Speaker: Michael Sergeant

HFW Seminar
Construction Projects: Actions to protect against counterparty insolvency
Perth, HFW Office
23 September 2020
Speaker: Matthew Blycha

HFW Offshore Wind Webinar Autumn Series
Design and Performance obligations and pitfalls
6 October 2020 (9am - 10am BST)
Speakers: Michael Sergeant, Richard Booth, Katherine Doran

HFW Seminar
The role of the Marine Warranty Surveyor and how should this be dealt with in offshore construction contracts
Perth, HFW Office
13 October 2020
Speaker: Matthew Blycha, Hazel Brewer

HFW Offshore Wind Webinar Autumn Series
Who takes the risk of the Marine Warranty Surveyor and how should this be dealt with in the construction contract?
20 October 2020 (9am - 10am BST)
Speakers: Max Wieliczko, Joanne Button, Chris Philpot

Renewable UK Global Offshore Wind 2020 Webinar
Case study: Liability for the Gwynt Y Mor OWF Export Cable Failures
28-30 October 2020
Speaker: Richard Booth

If you have any queries regarding any of these upcoming events, or to register your interest in attending, please contact us at events@hfw.com.

HFW has over 600 lawyers working in offices across the Americas, Europe, the Middle East and Asia Pacific. For further information about our construction capabilities, please visit hfw.com/construction

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