Parsons Plastics (Research and Development) Ltd. v Purac Ltd. [2002] Adj.L.R. 04/12

CA before : Lord Justice Pill, Lord Justice Mummery and Lord Justice Latham : 12th April 2002

JUDGMENT: LORD JUSTICE PILL:

1. This is an appeal from judgments of Her Honour Judge Kirkham given in the Technology and Construction Court, sitting in Birmingham, and dated 13 and 21 August 2001. Parsons Plastics (Research & Development) Ltd ("*the appellants*") were refused summary judgment in the sum of £222,765.75 (plus VAT and interest) against Purac Ltd ("the respondents") and a stay to arbitration of the respondents' Part 20 money claim. The judge granted the respondents summary judgment on their specific money claim. She ordered an interim payment of £12,000. The appellants were ordered to pay the respondents' costs.

2. The respondents were engaged by Anglian Water Service as main contractors for the design and construction of a sewage treatment works at Lowestoft. The respondents engaged the appellants as sub-contractors, under a written contract, for the supply of an odour control package at the works. Work under the sub-contract began in July 2000 although the sub-contract was not signed until 3 October 2000.

3. Concern was expressed about the appellants' lack of progress in the work and matters came to a head in December 2000. On 30 November 2000, at the request of the appellants, the respondents paid a sum of £30,963 direct to the appellants' steel supplier. By letter dated 11 December 2000 the appellants requested the respondents to make a further direct payment to their suppliers in the sum of about £100,000. That sum was not paid but the respondents agreed to some rescheduling. On 20 December 2000 the appellants applied for payment number 3 of a series of payments due when certain milestones, set out in the third schedule to the written agreement, had been reached. A total sum of £261,749.76 was claimed. The respondents declined to pay that sum claiming on 21 December that the sub-contract works had not reached the required stage. The respondents also claimed that the appellants had failed to meet delivery dates and, following warning letters, wrote to the appellants on 11 January 2001 purporting to give notice that they were taking over the remaining part of the sub-contract works (pursuant to Clause 20(c) of the sub-contract) on the ground that the appellants had failed to comply with their obligations under the contract. On 12 January 2001 the respondents ejected the appellants from the site. On 4 April 2001, the appellants referred the dispute as to whether they were entitled to payment under application number 3 to adjudication. Mr Daniel Atkinson FICE, FCIArb, accepted appointment as adjudicator on the following day.

4. An issue arose upon the jurisdiction of the adjudicator on the ground that the relevant work was not a "*construction operation*" as defined by the Housing Grants, Construction and Regeneration Act 1996 ("*the Act*"). During submissions about jurisdiction, the respondents' solicitor stated in writing, on 3 May 2001:

   "... we confirm that our client is prepared to submit to your jurisdiction under the terms of the sub-contract only, in respect of the dispute referred to you.

   It is out clients position that you would not have jurisdiction to conduct an adjudication in relation to this issue under the provisions of [the Act] for the reasons set out in our letter of 2nd May but notwithstanding this, our client is prepared to submit to your jurisdiction in respect of an adjudication of matters properly referred to you to be conducted under and in accordance with the provisions of the contract between the parties ..."

5. Notwithstanding that form of acceptance, the adjudicator did rule on the question whether the work was a "construction operation" within the meaning of the Act and concluded on 4 May 2001 that it was not. It was common ground that the Act did not apply to the adjudication.

6. On 17 May 2001 in the appellants' favour, the Adjudicator found that they were entitled to payment under Clause 17(a) of the sub-contract in respect of individual tasks which had been completed rather than having to wait until the whole of the sub-contract works had been completed. The appellants were held to be entitled to payment of 40% of the value of the completed activities. The respondents were ordered to pay the sum claimed plus interest. The Adjudicator also held that the respondents' letter of 21 December 2000 was not a payment notice within the meaning of Clause 17(e) of the contract or a withholding notice within the meaning of Clause 17(g). He also held that he did not have

jurisdiction to decide issues arising out of the respondents' letter of 11 January 2001. The Adjudicator's final decision was given on 17 May 2001.

7. On 23 May 2001, the respondents served notice, pursuant to Clause 17(g) of the contract, of intention to withhold payment of the sum awarded. They claimed that having taken over the sub-contract works pursuant to Clause 20(c), they were entitled to deduct from monies otherwise due to the appellants the reasonable cost of completing the works. The respondents had paid £303,000 plus VAT to Aderley Process Technologies Ltd ("APT") to complete the work. That was a larger sum than the sum awarded by the adjudicator and the appellants were not entitled to any payment, it was submitted.

8. The present proceedings were instituted by the appellants on 24 May 2001 to enforce the adjudicator's decision. The issue was whether the defence of set-off was available to the respondents. The appellants conceded that, if it was available, the respondents had an arguable counterclaim based on their allegations that the appellants were in breach of contract in failing to do the work in time and that, under the contract, the respondents were entitled to engage APT to complete the work at the sum agreed with them. It was also claimed by the respondents that the sum of over £30,000 paid to a third party on 30 November 2000 could be set off against the appellants' claim or form the basis for a counterclaim. The respondents sought summary judgment in respect of the sums of £303,000 paid or payable to APT and the £30,963 paid to the appellants' steel supplier. An interim payment was sought having regard to the excess of the respondents' claim over that of the appellants.

9. The appellants submit that the adjudication, while an ad hoc referral, was under the procedure set out in Clause 27 of the contract. The decision of the adjudicator was "final and binding" pursuant to Clause 27 of the contract and should be enforced by the Court as if the Act applied. Further, a set-off could only be taken into account if the procedure set out in Clause 17(g) of the sub-contract had been followed and the respondents had failed to serve a withholding notice in accordance with the Clause.

10. The relevant provisions of the sub-contract, as set out in the judgment of Judge Kirkham, and with the addition of the first paragraph of Clause 27a are:

"Clause 1 sets out various definitions, including

'1f. "Adjudicator" means the person referred to and so called in Clause 27

1g. "Sub-Contract Dispute" means any disagreement or difference between [Parsons] and [Purac] arising under the Sub-Contract in relation to any matter in connection with a "construction operation" as defined in the [Act] including any dispute as to whether the matter referred to the Adjudicator is in connection with a Construction Operation. ...

1m. "Final Date for Payment" means the date determined in accordance with Clause 17(h)(1).

17f. Subject to Clauses 11(e), 11(f), 20(c) and 31 and as hereinafter provided and without prejudice to any rights which exist [Purac] shall be entitled to withhold or defer payment of all or part of any sums otherwise due under the provisions hereof where:

i. any work done or Plant supplied by [Parsons] is not in accordance with the Sub-Contract then [Purac] may withhold the cost and expense of making good the defect in question. If without reasonable cause [Parsons'] performance of the Sub-Contract falls behind the approved programme of work then [Purac] may withhold the reasonable value of the Sub-Contract Works which ought to have been performed in accordance with the approved programme of work but which at the relevant stage in the programme of work remained undone.

ii. A dispute arises or has arisen between [Parsons] and/or [Purac] and the Purchaser involving any question of any matter included in any such application.

17 g. If [Purac] intends to withhold payment of a sum that has become due under the Sub-Contract in connection with a Construction Operation or otherwise then not later than one day before the Final Date For Payment of that sum [Purac] shall serve a notice specifying:

a) the amount proposed to be withheld and the ground for withholding payment or

b) if there is more than one ground, each ground and the amount attributable to it.

Provided that such notice will not be required if the notice mentioned in Clause 17e complies with the requirements in sub clauses (a) and (b) above.

17h. (i) [Purac] shall pay [Parsons] any amount due under the Sub-Contract 14 days after the date upon which the sum became due (the Final Date for Payment). Provided that where the matter in respect of which payment is to be made is not a "construction operation" within the definition provided by the Housing Grants Construction and Regeneration Act 1996 or the Purchaser becomes insolvent within the definition of "insolvent" provided by section 113 of the Housing Grants Construction and Regeneration Act 1996 [Purac] shall have no obligation to make any payment to [Parsons] except to make payment within 14 days after the date upon which [Purac] receives payment in respect of the sum due in respect of the sub-contract works.

20 a. If [Parsons]:

i. fails to proceed with the Sub-Contract Works with due diligence; or

ii. fails to execute the Sub-Contract Works or to perform his other obligations in accordance with the Sub-Contract; or

iii. refuses or neglects to remove defective materials or make good defective work after being directed in writing so to do by [Purac]; or

iv. commits an act of bankruptcy or enters into a deed of arrangement with his creditors or, being a company calls a meeting of its creditors, becomes subject to an Administration order, has a receiver appointed to manage its affairs by the holder of a charge or debenture or has a liquidator appointed, (other than a voluntary liquidation for the purposes of reconstruction), then in any such event and without prejudice to any other rights or remedies, [Purac] may by written notice to [Parsons] forthwith to determine [Parsons'] employment under this Sub-Contract and thereupon [Purac] may taken possession of all materials, plant and other things whatsoever brought on to the Site or in respect of which [Parsons] has received payment under Clause 17 and may use them for the purpose of executing, completing and maintaining the Sub-Contract Works and may, if he thinks fit, sell all or any of them and apply the proceeds in or towards the satisfaction of monies otherwise due to him from [Parsons].

b. Upon such a determination, the rights and liabilities of [Purac] and [Parsons] shall, subject to the preceding Sub-Clause, be the same as if [Parsons] had repudiated this Sub-Contract and [Purac] had by his notice of determination under the preceding Sub-Clause elected to accept such repudiation.

c. [Purac] may in lieu of giving a notice of determination under this Clause take part only of the Sub-Contract Works out of the hands of [Parsons] and may by himself, his servants or agents, execute, complete and maintain such part and in such event [Purac] may recover his reasonable costs of doing so from [Parsons], or deduct such costs from monies otherwise becoming due to [Parsons].

Clause 27 sets out a procedure for adjudication. It is a bespoke adjudication scheme, but is compliant with S. 108 of the Act.

27 a. Either party shall have the right to refer any sub-contract dispute for adjudication in accordance with the procedure set out in this Clause ... .

27 g. The decision of the Adjudicator shall he complied with forthwith upon receipt.

[DELETE ONE OF THE FOLLOWING BEFORE ISSUING TENDER]

h. (i) The decision of the Adjudicator shall be final and binding; or

(ii) The decision of the Adjudicator shall be binding on the parties and they shall comply with it until the dispute is finally determined by legal proceedings, by arbitration or by agreement between the parties.

(iii) If one of the above options 27h(i) or 27h(ii) has not been deleted then 27h(i) shall apply.

[Neither (i) nor (ii) had been deleted.

28 a. Where Clause 27h(i) does not apply and subject to the provisions of Clause 27 herein if any dispute arises between [Purac] and [Parsons] in connection with this Sub-Contract, it shall, subject to the provisions of this Clause, be referred to arbitration. ...

31. Nothing contained in this Deed whether expressly or by incorporation or by implication shall in any way restrict [Purac's] equitable or common law rights of set off. Without prejudice to the generality of the foregoing, [Purac] shall have the right to set off against any sum due to [Parsons] whether hereunder or otherwise a fair and reasonable sum in respect of or on account of any claim or claims that have been made

or which are to be made against [Purac] by the Purchaser the subject matter of which touches or concerns the Sub-Contract Works.'"

Appellants' claim for summary judgment

11. The appellants submit that the referral to adjudication was on the basis that the decision of the adjudicator should be "final and binding" under Clause 27h(i) and that the decision "shall be complied with forthwith upon receipt" under Clause 27g. While the adjudication was not under the Act it should be treated as if given under the Act to the extent that the terms of the sub-contract should be construed on the basis that the parties intended a swift resolution of disputes. The respondents had not complied with the contractual procedure which would have enabled them to set-off (Clause 17g).

12. The adjudicator had found, and it is accepted that his finding is not susceptible to challenge, that no Clause 17g notice was served by 16 February, that is the date by which, on the adjudicator's finding, the sum he found due on adjudication was payable. The respondents submit, however, that they have followed the procedure under Clause 17g by their notice of 23 May 2001 which was given before they were obliged to give effect to the adjudicator's final decision of 17 May. They make the further, and more basic, point that the procedure specified in Clauses 17f and 17g is expressly made subject to Clause 31 which preserves the respondents' equitable and common law rights of set-off. In **Modern Engineering v Gilbert-Ash** [1974] AC 689, 718E, Lord Diplock stated: *"So when one is concerned with a building contract one starts with the presumption that each party is to be entitled to all those remedies for its breach as would arise by operation of law, including the remedy of setting up a breach of warranty in diminution or extinction of the price of material supplied or work executed under the contract. To rebut that presumption one must be able to find in the contract clear unequivocal words in which the parties have expressed their agreement that this remedy shall not be available in respect of breaches of that particular contract."*

13. The appellants respond that Clause 31 merely restates the position under the contract and is declaratory of rights expressed in the contract. Moreover, if it was to be relied on, it was necessary to follow the procedure in Clause 17g. A Clause similar in wording to Clause 17g appears in the form of sub-contract issued by the Civil Engineering Contractors Association (October 1998) but there is no equivalent of Clause 31 in that form. In support of the submission that Clause 31 does not provide an overriding contractual right to set-off, reference is made to the fact that the expression "subject to Clause 31" does not expressly govern Clause 17g which provides a procedure, it is submitted, which must be followed whenever a right to set-off is claimed to negative the obligation under Clause 27g. Upon the submission to the adjudicator in fact made, Clause 27g operates to require compliance with his decision forthwith.

14. I have not found the question an easy one. When parties provide, in this context, a specific procedure by which a claim to withhold payment is to be notified (and detailed), it cannot readily be concluded that the effect of a general Clause such as Clause 31 is to make the procedure unnecessary.

15. I have, however, come to the conclusion that failure to give a notice under Clause 17g is not fatal to the respondents' right to set-off. Clauses 17f and 17g must be read together, 17g providing a mechanism whereby the respondents can exercise the right conferred in 17f. The expression "subject to Clause 31" governs both paragraphs and preserves the expressed preservation of rights of set-off in Clause 31. The expression "nothing contained in this deed shall in any way restrict" in Clause 31 is consistent with the procedure in Clause 17g being subject to it. In my view, the judge reached the correct conclusion. It is open to the respondents to set-off against the adjudicator's decision any other claim they have against the appellants which had not been determined by the adjudicator. The adjudicator's decision cannot be re-litigated in other proceedings but, on the wording of this sub-contract, can be made subject to set-off and counterclaim. It is accepted that the respondents' counterclaim, if they are entitled under the terms of the sub-contract to set it off against the claim, is arguable.

16. If that approach is correct, it is unnecessary to decide whether the purported notice of 23 May 2001 complied with Clause 17g of the sub-contract. The notice must be served *"not later than one day before the final date for payment"* in respect of a sum "that has become due under the sub-contract". The *"final date for payment"* is defined in Clause 17h as being *"14 days after the date upon which the sum became due"*.

On behalf of the respondents, it is submitted that the sum became due upon the adjudicator's final decision on 17 May 2001. The judge held that *"the sum claimed [by the appellants] is a sum determined by the adjudicator, it is not a sum due under the sub-contract. Accordingly, it falls outwith the definition of 'before final date for payment'."*

17. I do not propose to decide the point and would need to consider further the provisions in the sub-contract as to money becoming due before doing so. I do however express my doubts about both the propositions set out in the previous paragraph. The fact that it is an adjudicator who decides that the payment should be made does not on the face of it make it any less due under the sub-contract which has provided for his appointment. It may also have become due under the sub-contract on a particular date even if that date is only determined by the adjudicator at a later date. I leave the point open.

18. The extent of the right to set-off under Clause 17f does not, on my findings, arise.

Application to stay respondents' claim to arbitration.

19. The appellants submit that Clause 28 of the sub-contract is a binding arbitration clause. The dispute raised upon the respondents' claim was entirely separate from that determined by ad hoc adjudication. The respondents' claim was not submitted to adjudication. Moreover, Clause 27 could have no application because (notwithstanding the appellants' reliance on Clause 27 on other issues), the work was not a "construction operation" within the meaning of Clause 1g and Clause 27. That being so, it is submitted, Clause 28 should be read as if Clause 27 was not present in the contract and provides a binding arbitration clause.

20. I cannot accept that submission. The fact that it was later decided by an adjudicator that the sub-contract work was not a construction operation does not permit a party to treat the sub-contract as if Clause 27 was absent so that the reference to it in Clause 28a can be ignored. The opening words of Clause 28a refer to Clause 27 and require arbitration only "where Clause 27h(i) does not apply". When the parties entered into the contract they did not delete Clause 27h(i) with the result that by virtue of Clause 27h(iii) that paragraph "shall apply". Clause 28a can, by the terms, operate only where Clause 27h(i) does not apply.

Judgment on Part 20 claim and interim payment

21. It is conceded that upon proof of a relevant breach of contract under Clause 20 the respondents were entitled to take the remainder of the sub-contract works out of the hands of the appellants under Clause 20c. The sub-Clause was probably intended primarily to apply to a situation where a part of the works was to be left with the sub-contractor but it is agreed that the Clause is capable of covering the circumstances of this case. The issues arising were essentially issues of fact for the judge. It is submitted that by using the expression "on balance" in relation to the respondents' entitlement to invoke Clause 20c, the judge has applied the wrong test to an application for summary judgment (**Swain v Hillman** [2001] 1 All ER 91). The judge erred in conducting a "mini trial", it is submitted. It is further submitted that there was evidence that the appellants' performance of the sub-contract was delayed or prevented by the conduct of other sub-contractors and also that no loss arose from any delay by the appellants because other sub-contractors were not ready to accommodate the appellants' work.

22. I do not consider that the judge's use of the expression *"on balance"* affects the validity of her conclusion. She plainly had in mind the correct test and referred to **Swain v Hillman**. In her judgment of 21 August 2001, the judge carefully considered the considerable evidence before her. The appellants' own material revealed substantial breaches of the obligations in Clause 20. The judge rightly held that the issue was whether the breaches entitled the respondents to take over the work pursuant to the Clause and questions as to whether the appellants' delays were causative of other delays were not relevant. The judge was entitled to conclude that the appellants *had "no real prospect of successfully defending [the respondents'] claim"* for the cost of completing the work. She noted that the respondents' entitlement to credit for payment to the steel supplier was not disputed. There was no error of law by the judge and she was entitled, on the evidence, to reach the conclusion that the respondents were entitled, to the extent of those two claims, to summary judgment.

23. Moreover, on the material before her, the judge was entitled, in her discretion, to make an interim award of £12,000 in the respondents favour. The judge acknowledged that credit should be given to the appellants for the amount awarded to them by the adjudicator. The figures were such that a modest interim award could properly be made. Amongst other things, the appellants' calculation of the value of outstanding work was close to the sum of £303,000 held to be payable to APT. There was a substantial difference, in the respondents' favour, between the amount claimed by them and the amount claimed by the appellants.

24. I would dismiss the appeal.

Lord Justice Mummery:

25. I agree.

Lord Justice Latham:

26. I also agree.

Paul Bleasdale QC and Peter Collie (instructed by Paris & Co) for the Appellants

Anthony Edwards-Stuart QC and Andrew Rigney (instructed by Masons) for the Respondents