

**Melville Dundas Ltd (in receivership), Colin Peter Dempster & Thomas Merchant v George Wimpey UK Ltd
Norwich Union Insurance Ltd Third Party:**

OPINION OF LORD CLARKE : Outer House Court of Session : 22nd October 2004

- [1] The dispute in this commercial action arises out of a construction contract, under which the first named pursuers were engaged to carry out the design and construction of a housing development on behalf of the defenders. The contract entered into between the first named pursuers and the defenders, was on the terms of the Standard Form of Building Contract issued by the Scottish Building Committee, known as the "*Scottish Building Contract With Contractor's Design Section on Completion Edition*" in the January 2000 version of its May 1999 edition.
- [2] In the present action, the pursuers seek payment of the sum of £396,630, together with interest thereon from 17 May 2003, which sum they claim is due to them by the defenders in terms of the said contract. The defenders deny that the said sum is due to be paid to the pursuers. The third party was convened to the proceedings by the defenders, on the basis that, *esto* the defenders are liable to the pursuers for the sum in question, they are entitled to recover payment of any such sum from the third party under a performance bond issued by the third party in favour of the defenders. The case came before me for debate on all the parties' preliminary pleas, as to the relevancy and specification.
- [3] The basis of the pursuers' claim is to be found in clause 30 of the said contract which is concerned with interim payments. The provisions of that clause are somewhat elaborate and complex. The following specific provisions are relevant for present purposes. Clause 30.1.1. provides:
"Interim Payments shall be made by the Employer to the Contractor in accordance with clause 30.1. to 30.4 and whichever of the Alternatives A or B in Appendix 2 applies to this Contract."

It was a matter of agreement among the parties that Appendix B applies to the contract in question. Clause 30.3.1. provides:

*"The Contractor shall make Applications for Interim Payment as follows: ...
where Alternative B applies, Application for Interim Payment shall be made at the Period for Applications for Interim Payment stated in Alternative B in Appendix 2 up to and including the end of the period during which the day named in the Statement of Practical Completion occurs. Thereafter Application for Interim Payment shall be made as and when further amounts are due to the Contractor and after the expiration of the Defects Liability Period named in Appendix 1 or on the issue of the Notice of Completion of Making Good Defects (whichever is the later) provided that the Employer shall not be required to make any Interim Payment within one calendar month of having made a previous Interim Payment."*

Clause 30.3.2 then provides:

"Each application for Interim Payment shall be accompanied by such details as may be stated in the Employer's Requirements."

Clause 30.3.4. goes onto provide as follows:

"Not later than 5 days before the final date for payment of an amount due pursuant to clause 30.3.3 the Employer may give a written notice to the Contractor which shall specify any amount proposed to be withheld and/or deducted from that due amount, the ground or grounds for such withholding and/or deduction and the amount of withholding and/or deduction attributable to each ground."

Clause 30.3.5 then states:

"Where the employer does not give any written notice pursuant to clause 30.3.3. and/or to clause 30.3.4, the Employer shall pay the Contractor the amount stated in the Application for Interim Payment."

Clause 30.3.6 is to the following effect:

"The final date for payment of an amount due in an Interim Payment shall be 14 days from the date of receipt by the Employer of the Contractor's Application for Interim Payment."

In Article 4 of condescendence the pursuers aver, *inter alia*, as follows,

"Clause 4 of the said Scottish Building Contract, as completed by the parties, made Messrs. Robinson Low Francis, Claremont House, 20 North Claremont Street, Glasgow, the agent of the defenders for the purpose of receiving or issuing applications or notices under any of the conditions of the contract. The pursuers duly

commenced the works entrusted to it under the said contract, and, on 2 May 2003, following the procedure in the said clause 4, it submitted to the defenders' said agents, Messrs. Robinson Low Francis, an Application for Interim Payment (No.20) for the work done by the pursuers from the time of its eighteenth application for interim payment down to 30 April 2003. The same day, Messrs. Robinson Low Francis issued a Valuation No.20, certifying that the sum in which they valued (at the rates and prices provided for in said contract) the work done by the pursuers between the date of their interim certificate 19 and 30 April 2003 was £396,630, exclusive of VAT. A copy of that Valuation was issued to the pursuers, which thereupon invoiced the defenders for payment of the said £396,630, that sum attracting, in the circumstances, no VAT. No notice under either sub-clause 30.3.3 or sub-clause 30.3.4 of the said contract, has been served on the pursuers by the defenders in respect of the said £396,630, or any part thereof. Accordingly, that sum became due by the defenders to the pursuers on 2 May and overdue for payment on 17 May 2003, following the passing of the final date for payment in respect of said sum."

[4] It was accepted, on behalf of the defenders, that no notices were served by them, or anyone on their behalf, in terms of clause 30.3.3 or 30.3.4 of the contract. It was accepted, furthermore, on behalf of the defenders, that the said sum sued for was, in terms of clause 30, due to be paid no later than 16 May 2003. Nevertheless the defenders, and the third party, resist payment of the said sum, in the present action, because of the operation of a separate chapter of the contract, namely the provisions of clause 27 thereof. Clause 27 is headed "Determination by Employer".

[5] It is a matter of agreement among the parties that on 22 May 2003, the first named pursuers had receivers appointed to them. Clause 27.3.1, 27.3.3 and 27.3.4 of the contract provide:

"27.3.1 If the Contractor -

makes a composition or arrangement with his creditors, or becomes bankrupt, or being a company,

makes a proposal for a voluntary arrangement for a composition of debts or scheme of arrangement to be approved in accordance with Companies Act 1985 or the Insolvency Act 1986 as the case may be, or any amendment or re-enactment thereof, or

has a provisional liquidator appointed, or

has a winding up order made, or

passes a resolution for voluntary winding up (except for the purposes of amalgamation or reconstruction) or

under the Insolvency Act 1986 or any amendment or re-enactment thereof has an administrator or administrative receiver appointed

then:

...

27.3.3 Where a provisional liquidator or trustee in bankruptcy is appointed or a winding up order is made or the Contractor passes a resolution for voluntarily winding up (except for the purposes of amalgamation or reconstruction) the employment of the Contractor under this Contract shall be forthwith automatically determined but the said employment may be reinstated if the Employer and the Contractor (v) shall so agree;

27.3.4. where clause 27.3.3 does not apply, the Employer may at any time, unless an agreement to which clause 27.5.2.1 refers has been made, by notice to the Contractor determine the employment of the Contractor under this contract and such determination shall take effect on the date of the receipt of such notice."

It is a matter of further agreement among the parties that on 30 May 2003 the defenders, by notice in terms of clause 27.3.4, determined the employment of the first named pursuers. In that situation, in terms of the contract, the provisions of clause 27.5.1 come into play. They are as follows:

"27.5.1 From the date when, under clause 27.3.4, the Employer could first give notice to determine the employment of the Contractor, the Employer, subject to clause 27.5.3, shall not be bound by any provisions of this Contract to make any further payment thereunder and the Contractor shall not be bound to continue to carry out and complete the design and construction of the Works, in compliance with clause 2.1."

The date when the defenders, as employer, could first have given notice to determine was 22 May 2003.

The provisions of clause 27.6.5 are also of relevance for present purposes. They are in the following terms:

"27.6.5.1 Subject to clauses 27.5.3. and 27.6.5.2 the provisions of this Contract which require any further payment or any release or further release of Retention to the Contractor shall not apply; provided that clause 27.6.5.1 shall not be construed as to prevent the enforcement by the Contractor of any rights under this Contract in respect of amounts properly due to be paid by the Employer to the Contractor which the Employer has unreasonably not paid and which, where clause 27.3.4 applies, have accrued 28 days or more before the date when under clause 27.3.4 the Employer could first give notice to determine the employment of the Contractor or, where clause 27.3.4 does not apply, which had accrued 28 days or more before the date of determination of the employment of Contractor.

27.6.5.2 Upon the completion of the design and construction of the Works and the making good of defects as referred to in clause 27.6.2 (but subject, where relevant, to the exercise of the right under clause 16.2 and/or clause 16.3 of the Employer not to require defects of the kind referred to in clause 16 to be made good), then within a reasonable time thereafter an account in respect of the matters referred to in clause 27.6.6 shall be set out in a statement prepared by the Employer."

- [6] The position of the defenders and the third party at the debate before me, as to the effect of these last mentioned provisions, was as follows. It was contended that the provisions meant that, while the contractor was entitled to demand payment of sums which had become due and which had accrued to him for at least 28 days before 22 May 2003, i.e. the first day upon which the employer could have given the necessary notice, payment of sums which had not become due and had accrued to the contractor within that period, could no longer be demanded by the contractor. The sum which the pursuers sued for, in the present case, had not accrued to the pursuers, at least 28 days before the first day on which notice of determination by the defenders could have been given. That was, therefore, a sum, payment of which the first named pursuers were not entitled to sue for, at this time, because of the provisions of clause 27.5.1. It was pointed out that by virtue of clause 27.6.2, where there was a determination of the employment of the contractor, as has happened in this case;

"The Employer may employ and pay other persons to carry out and complete the design and construction of the Works and to make good defects of the kind referred to in clause 16 and he or they may enter upon the site and the Works and use all temporary buildings, plant, tools, equipment and Site Materials, and may purchase all materials and goods necessary for the carrying out and completion of the Works and for the making good of defects as aforesaid provided that where the aforesaid temporary buildings, plant, tools, equipment and Site Materials are not owned by the Contractor, the consent of the owner thereof to such use is obtained by the Employer."

The provisions of clause 27.6.7 provide that, in the event of a determination of the contract, as has occurred in the present case, there shall be a balancing exercise to be carried out to arrive at the sums due to the contractor by the employer or by the contractor to the employer, as the case may be.

- [7] In the discussion before me, senior counsel for the pursuers, accepted that, if the question as to the pursuers' entitlement to be paid the sum sued for under the interim certificate turned on an analysis of the contractual provisions, just referred to, then he was not in a position to contradict the construction and the effect of the provisions which the defenders and the third party advanced. What altered the position, however, in the pursuers' favour, were the statutory provisions to be found in the Housing Grants, Construction and Regeneration Act 1996, sections 109, 110 and 111. Section 109 of the Act is to the following effect:

"(1) A party to a construction contract is entitled to payment by instalments, stage payments or other periodic payments for any work under the contract unless -

(a) it is specified in the contract that the duration of the work is to be less than 45 days, or

(b) it is agreed between the parties that the duration of the work is estimated to be less than 45 days.

(2) The parties are free to agree the amounts of the payments and the intervals at which, or circumstances in which, they become due.

(3) In the absence of such agreement, the relevant provisions of the Scheme for Construction Contracts apply.

(4) Reference in the following sections to a payment under the contract include a payment by virtue of this section."

Section 110 of the Act provides as follows:

"(1) Every construction contract shall -

(a) provide an adequate mechanism for determining what payments become due under the contract, and when, and,

(b) provide for a final date for payment in relation to any sum which becomes due.

The parties are free to agree how long the period is to be between the date on which a sum becomes due and the final date for payment.

(2) Every construction contract shall provide for the giving of notice by a party not later than five days after the date on which a payment becomes due from him under the contract, or would have become due if -

(a) the other party had carried out his obligations under the contract, and

(b) no set off or abatement was permitted by reference to any sum claimed to be due under one or more other contracts,

specifying the amount (if any) of the payment made or proposed to be made, and the basis on which that amount was calculated.

(3) If or to the extent that a contract does not contain such provision as is mentioned in subsection (1) or (2), the relevant provisions of the Scheme for Construction Contracts apply."

Section 111 is, *inter alia*, to the following:

"(1) A party to a construction contract may not withhold payment after the final date for payment of a sum due under the contract unless he has given an effective notice of intention to withhold payment ..."

[8] The pursuers' argument based on those provisions, was to the following effect. Clause 27 of the contract operated as a suspension of payment, until the balancing exercise provided for under that clause had been gone through, and the netting off cross-claims had been processed. That was, in effect, providing for a scheme for withholding payment. The defenders did not aver that any effective notice of intention to withhold payment of the sum in question, in accordance with the provisions of section 111 had been given by them. That being so, the effect of the statutory scheme was that the defenders could not withhold the payment in question. Clause 27 had to be read so as to avoid conflict with section 111, if possible. If that was not possible, the relevant provisions of clause 27 had to be struck down.

[9] The defenders' response to this argument was as follows. The provisions of clause 30.3.3 of the contract, reflected the requirements of section 110(2) of the 1996 Act. The provisions of clause 30.3.4 of the contract, reflected the requirements of section 111. The critical words in section 111(1), for the purposes of the present dispute, were "The final date for payment of a sum due under the contract." It was submitted, on behalf of the defenders, and the third party, that the statutory provisions left the parties free to determine, as a matter of contract, what sums were due under that contract and in what circumstances. In the present case, the parties had determined, by agreement, that even if a sum was due before a receiver was appointed to the contractor then, if the contract was determined by the employer, as a result of the appointment of the receiver, by virtue of a notice given by the employer in terms of clause 27.3.4, then the only sums remaining due and payable thereafter, were those provided by virtue of clause 27.6.5.1. The statutory provisions had not restricted the parties freedom to contract to that effect. In respect of the metes and bounds of the provision contained in section 111, I was referred to what Lord Macfadyen said in the case of *S L Timber Systems Ltd v Carillion Construction Ltd* 2002 SLT 997, where, at pages 1002-1003, His Lordship said:

"The more significant issue in the present case, in my opinion, is whether the defenders' failure to give a timeous notice under section 111 had the effect that there could be no dispute at all before the adjudicator as to whether the sums claimed by the pursuers were payable. The section provides that a party 'may not withhold payment after the final date for payment of the sum due under the contract unless he has given an effective notice of intention to withhold payment'. In my opinion the words 'sums due under the contract' cannot be equiperated with the words 'sum claimed'. The section is not, in my opinion, concerned with every refusal on the part of one party to pay a sum claimed by the other. It is concerned, rather, with the situation where a sum is due under the contract, and the party by whom that sum is due seeks to withhold payment on some separate ground."

- [10] That dictum, it was submitted, pointed to the fact that section 111 was not concerned with prescribing what sums were due under the contract. That was a matter which the parties to the contract themselves had to provide for. I was referred also to the decision in the case of *Rupert Morgan Building Services (LLC) Ltd v Jervis &c* (2003) EWCA Civ 1563. It was submitted, on behalf of the defenders, that a withholding notice, in terms of section 111 could not have been issued timeously, in the present case, because the insolvency of the first named pursuers occurred immediately after the date of the expiry of the period during which such a notice should have been issued. That practical problem, in itself, pointed against the approach contended for by the pursuers.
- [11] For the pursuers, it was submitted that in seeking to operate the provisions of clause 27, the defenders were creating, in effect, a security fund to protect themselves in the light of the pursuers' insolvency. The right to do this had, it was submitted, been swept away by the legislative provisions. Senior counsel for the pursuers, however, accepted that ultimately the question in the instant case was whether, notwithstanding the provisions of section 111 of the 1996 Act, the parties, by virtue of the provisions of the contract, remain free to alter an agreed date of payment of a sum certified to be payable under the terms of the contract, to another date, in the light of the determination of the contract.

Decision

- [12] I am satisfied that the pursuers' case is irrelevant and falls to be dismissed. As has been noted, senior counsel for the pursuers accepted that, but for the provisions of section 111 of the 1996 Act, the pursuers would not have been entitled to claim the payment of the sum in question in these proceedings, since the effect of clause 27 and the notice of determination of the contract issued by the defenders was that, as a matter of contract, the employer was not bound to pay the sum in question and that questions of further payment were to be resolved under the balancing exercise provided for in clause 27. The question was, then, whether the provisions of section 111 subverts these contractual arrangements. I am satisfied that the provisions of section 111 do not have that effect. Section 109, section 110 and section 111 of the 1996 Act are, in my judgment, concerned with, and directed, at cash-flow questions, arising during the course of a continuing, non-determined construction contract. I agree with the defenders, and third party, that the provisions of clause 30 reflect the requirements of section 110 and section 111. Clause 27, however, is concerned, with a quite different situation i.e. where the contract is legitimately determined by the employer. In my opinion, the legislative provisions were not intended to regulate that situation. That situation is one for which the parties themselves have legislated and their freedom of contract in that respect has, in my judgment, not been affected by the legislative provisions. The parties' continuing freedom of contract is expressly recognised in section 109(2) and, even more importantly, for present purposes, in section 110(1) where it is provided as follows: "*The parties are free to agree how long the period is to be between the date on which a sum became due and the **final date for payment.***" (My emphasis).
- [13] Putting the matter another way, in the present case, the parties were free to agree that the original date for payment of sums due under the contract, could be altered in the event of the contract being determined so that "the final date for payment" of the sum in question, has not, by reason of the contractual provisions yet arrived. In that situation section 111 upon which the pursuers base their case has no relevance. For the foregoing reasons I will sustain the defenders' first plea-in-law and the third party's first plea-in-law and dismiss the action.

Pursuers: Howie, Q.C.; Maclay Murray & Spens
Defenders: Currie, Q.C., Henderson; Lindsays, W.S.
Third Party: McNeil, Q.C.; MacRoberts