

Payment Notice Disputes and Cross Claims

*Wilson & Sharp Investments Ltd –v- Harbour View Developments Ltd*¹

Whilst this case contains multiple aspects that may be of interest to the construction practitioner, the purpose of this article is to focus on the relationship between the payment obligations which arise by virtue of the Construction Act² and the rights of Company A to wind up Company B due to a failure to meet the payment obligations which arise under the aforementioned legislation.

The salient facts are that Harbour View issued two interim applications for payment amounting to approximately £1.2 million. Wilson & Sharp failed to serve the right notices against these applications and as such a payment obligation was established. For those of you who may be unsure how such an obligation may arise, a brief summary is as follows;

The Construction Act and corresponding Scheme³ provides that a party cannot withhold payment beyond the final date for payment unless it has served a valid notice to that effect.

Although specifics may change from case to case, it is usually the form that the contractor makes an interim application for payment and the employer then has two opportunities to avoid paying this application in full (1) the issuing of a 'payment notice'; and (2) the issuing of a 'payless notice'. Should the employer fail to issue both of these notices within the requisite time, which is determined by the contract or the Act and Scheme (In this case the contract was a JCT Intermediate Building Contract with Contractor Design 2011. The provisions of which complied with the requirements of the Construction Act) then the full value of the contractor's application becomes the 'notified sum'. Pursuant to Section 111 of the Construction Act, the notified sum must be paid in full. No exceptions.

There was no disputing the fact that Wilson & Sharp had failed to issue the requisite notices. Harbour View then served a statutory demand seeking recovery of this notified sum.

Statutory demands are often used by commercial lawyers as a tool for 'encouraging' payment. They are a cheap way to apply pressure and seek recovery for outstanding debts since they threaten liquidation if the sum sought is not paid within 21 days. One can only speculate that this was the thinking behind Harbour View's approach.

The statutory demand obviously did not have the desired effect of scaring Wilson & Sharp to pay the outstanding sums, who instead sought an injunction restraining the presentation of a petition of winding up. This injunction was brought on the grounds that the interim certificates had grossly overvalued Harbour View's works.

The question therefore being considered by this article is; 'given the robust nature of the courts' application of the payment provisions within the Construction Act and Scheme, was the court prepared to allow Harbour View to petition for the winding up of Wilson & Sharp in this instance?'

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The law leading up to this case was fairly clear. In *Tallington Lakes Ltd and another v Ancasra International Boat Sales*⁴ the Court of Appeal considered when a court will strike out a winding up petition or restrain its presentation. It was held in this case that:

“If the company can demonstrate that the alleged debt on which the petition is founded is genuinely disputed on substantial grounds, the court will strike out the petition. There are rare exceptions to this principle...” [Justice Richards]

*Seawind Tankers Cooperation –v- Bayoils SA*⁵ established that if a debtor can establish a serious and genuine cross claim that exceeds the sum allegedly owed by it, then that is sufficient grounds for restraining the presentation of a winding up petition.

The Judge at first instance in *Wilson & Sharp* refused to grant the injunction restraining presentation of the winding up. One of the main reasons for this was that he did not believe that *Wilson & Sharp*'s cross claim was serious and genuine. He believed it was a “*put up*” job.

However, the Court of Appeal saw things differently (leaving aside factors concerning the insolvency of *Harbour View*), the Court of Appeal found that the failure to present a payless notice did not prevent *Wilson & Sharp* from raising a cross claim for over valuation and damages for repudiatory breach. The report of the quantity surveyor acting on behalf of *Wilson & Sharp* was deemed sufficient to establish an injunction, even though *Wilson & Sharp* had not litigated their cross claim.

The Court of Appeal also confirmed that the absence of a payless notice does not prevent an employer from arguing that the valuation in an interim certificate was wrong. This reasoning may arguably be extended to other proceedings within the Technology and Construction Court and not only those concerning winding up proceedings.

The Court of Appeal also confirmed that a winding up petition should not be used to enforce an interim payment obligation where that payment is challenged or there is a genuine cross claim. In determining the issue the employer will not be prejudiced by the absence of a payless notice or the fact that he has failed to commence adjudication, litigate or commence other proceedings against the Contractor if the employer has reasons for not doing so.

This case confirms that using winding up provisions to enforce interim payments is not the correct avenue to take. Adjudication followed by enforcement in the TCC is likely to be the more appropriate route.

¹ [2015] EWCA Civ 1030

² Housing Grants, Construction and Regeneration Act 1996 as amended by the Local Democracy, Economic Development and Construction Act 2009

³ The Scheme for Construction Contracts (England and Wales) Regulations 1998 as amended by the Scheme for Construction Contracts (England and Wales) Regulations 1998 (Amendment) (England) Regulations 2011

⁴ (2012) EWCA Civ 1712

⁵ [1998] EWCA Civ 1364

