

Update: Construction & Insolvency



Focus on
COVID-19
Coronavirus

Bresco Electrical Services Limited (In Liquidation) –v- Michael J Lonsdale (Electrical) Ltd:

Liquidators can refer a dispute to adjudication

1. Summary

The Supreme Court decision in Bresco Electrical Services Ltd (In Liquidation) –v- Michael J Lonsdale Electrical Ltd handed down on 17 June 2020 is both timely and significant given the “new normal” that we are all now operating within. In the current economic climate of “lockdown” and the present economic downturn that is now occurring, the worlds of construction and insolvency are now likely to interact and collide on a more frequent basis.

Bresco –v- Lonsdale is one such example of how the interaction of construction law and insolvency law can lead to important legal issues arising. In this case, the issues were of such significance and of general public importance that they progressed up to the Supreme Court in London.

The core issue in the case, centered on the compatibility of two different statutory regimes - the right to refer building disputes to construction adjudication vs the operation of insolvency set off.

The unanimous decision of the Supreme Court which allowed the appeal by the liquidators of Bresco was handed down by Lord Briggs. The decision now provides certainty to both those in the construction sector and also to insolvency practitioners that construction adjudication is not incompatible with the insolvency regime and indeed, is an important and fundamental statutory right that liquidators can pursue.

Practically speaking, this is a positive and important Judgment given the attraction of adjudication and the speedy process that is inherent in the adjudication regime. For liquidators operating in the current climate it is undoubtedly good news that the cost effective and quick nature of adjudication will be available to them to resolve disputes without recourse to the Courts with the time and expense that that often involves.

2. Background: Adjudication vs Insolvency Set Off

Adjudication

Adjudication is now widely recognised throughout the whole of the UK Construction Industry as a mainstream dispute resolution mechanism which involves the reference at any time of a dispute to an independent expert for a prompt decision within a limited period of time. The decision is then considered binding unless it is challenged by one of the parties in either arbitration or in Court. Importantly, however, the losing party has to comply with the decision in the interim – this is the principle of “pay now, argue later” which is centric to the overriding objective of adjudication in ensuring the protection of cashflow during construction works. This is now even more pertinent than ever in view of the prevailing gloomy current economic climate.

Insolvency Set Off

Insolvency set off in a liquidation is a relatively straightforward legal concept where there are mutual debts and credits they can cancel each other out leaving a single amount due to one of the parties. A liquidator often calculates this and decides who is owed what.

In Bresco –v- Lonsdale these two different statutory regimes collided.

In short, both Bresco and Lonsdale claimed monies from each other. Bresco entered into liquidation and the liquidator of Bresco sought to refer the dispute to adjudication. Lonsdale objected on the basis that they argued that the claims could just be offset via insolvency set off and on the basis that the adjudicator’s decision would be futile and a pointless exercise. Therefore the effect of Lonsdale’s arguments was that the adjudicator had no jurisdiction or authority whatsoever to entertain or determine this dispute.

Lonsdale succeeded at first instance and at the Court of Appeal. Bresco therefore appealed to the Supreme Court.

3. The Decision

The Supreme Court had to decide two principle issues:

1. Could an adjudication take place given the existence of insolvency?
2. If the process took place, would it be futile?

The Supreme Court unanimously held in Bresco's favour noting that while a court may decide not to enforce an award due to insolvency, it does not mean the option to adjudicate should be removed from the liquidator.

It was held that Bresco and its liquidator had a statutory, as well as a contractual right to adjudication and the Court refused to interfere with the exercise of these fundamental rights.

Lord Briggs best summed up the decision as follows:

"Construction adjudication, on the application of the liquidator, is not incompatible with the insolvency process. It is not an exercise in futility, either generally or merely because there are cross-claims falling within insolvency set-off, and there is no reason why the existence of such cross-claims can constitute a basis for denying to the company the right to submit disputes to adjudication which Parliament has chosen to confer."

One other significant part of the Judgment centres on Lord Briggs' comments around the enforcement of adjudicator's decisions. The Supreme Court indicated in this regard that enforcement could be subject to liquidators having to "ring fence" proceeds.

4. Commentary

The decision is **both** significant and timely.

While it may not always be the case that an insolvency practitioner will wish to pursue an adjudication, there is no reason why the option should not remain open to them and they now have that option.

In practice this may now result in an increase in adjudications as liquidators now seek to bring claims on behalf of companies in liquidation.

Given the economic downturn we are facing and the fact that adjudication has proved to be such a successful mechanism for dispute resolution within the construction industry, this may be a particularly important consideration for an insolvency practitioner. It will, however, be interesting to see how the lower courts now approach enforcement claims in light of the decision and the comments concerning undertakings/ring-fencing.

Whilst this Judgment now paves the way for them to do so we will have to wait and see how many liquidators go down the path of adjudication. But with an anticipated increase in insolvencies amongst the construction sector we can see that this Judgment is likely to have a number of implications as follows:

1. Adjudications that have been "waiting in the wings" now proceeding.
2. Potentially an increase in adjudications from companies in liquidation.
3. Liquidators being requested to provide undertakings to the Court.
4. Further enforcement challenges.

Our team

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