HARMONY AT LAST: THE SUPREME COURT'S DECISION IN BRESCO V LONSDALE

15 JULY 2020 • ARTICLE

The UK Supreme Court has handed down its much-anticipated decision in *Bresco v Lonsdale*[1], confirming that an adjudicator has jurisdiction to hear a dispute brought by an insolvent party, notwithstanding the existence of cross-claims. In rejecting the "trenchant" observations of specialist judges that the insolvency regime and the statutory adjudication regime are incompatible, the Supreme Court has firmly emphasised its support for adjudication, and the utility of the process beyond the "pay now argue later" principle. However, the insolvency of a party will still remain a potential barrier to enforcement of an adjudication award.

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BACKGROUND

Bresco and Lonsdale were both electrical works contractors. In 2014 Bresco agreed to perform works for Lonsdale at a site in London, but in 2015 Bresco entered into insolvent liquidation. At the time of Bresco's insolvency, both parties claimed that they were owed money by the other: Lonsdale argued that Bresco had prematurely abandoned the project, forcing it to pay for replacement contractors, whilst Bresco contended that it had never been paid by Lonsdale for some completed works.

In compliance with the requirements of section 108 of the Housing Grants, Construction and Regeneration Act 1996 the contract expressly provided for adjudication of disputes and so, following its insolvency, Bresco's liquidator referred its claim to adjudication. However, Lonsdale objected to adjudication on two grounds:

1. Because there were cross-claims between the parties and Bresco was insolvent, the claims were subject to the process of automatic set-off under the UK insolvency regime, which effectively replaced the cross-claims with a single claim for the net balance following the taking of an account. There was therefore no longer a claim, or dispute, under a construction contract pursuant to which an adjudication could be brought. Therefore, the adjudicator lacked jurisdiction; and
2. Even if the adjudicator had jurisdiction, any adjudication award was unlikely to be enforceable in the context of insolvency set-off and would therefore be "*an exercise in futility*" which the court should restrain by means of an injunction, in order to avoid wasted costs on a formal process which served no purpose.

Lonsdale commenced proceedings in the Technology and Construction Court and at first instance both arguments were upheld, and an injunction was granted to restrain the further conduct of the adjudication. The Court of Appeal subsequently reversed the first instance decision on jurisdiction but upheld the injunction on the grounds of futility. Lord Justice Coulson noted that adjudication is a method of obtaining improved cashflow quickly and cheaply. However, where an insolvent company has obtained an adjudication award in its favour, it will generally be unable to obtain judgment to enforce that award, or alternatively a stay on enforcement will be ordered, given the risk that the respondent will be unable to recover its money following any final determination of the dispute. Lord Justice Coulson therefore considered that a reference to adjudication in such circumstances would be incapable of enforcement and would be an exercise in futility. Bresco appealed to the Supreme Court to reverse the continuation of the injunction, whilst Lonsdale cross-appealed on the jurisdiction argument.

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DECISION

Jurisdiction

On Lonsdale's cross-appeal as to jurisdiction, the Supreme Court looked at the true construction of section 108 of the Act and the terms of the contract, which here incorporated the default provisions set out in the Scheme for Construction Contracts. Pursuant to such wording, a properly appointed adjudicator normally has jurisdiction to determine a dispute if it arises under the contract and has been referred to the adjudicator by one of the parties to the contract.

However, Lonsdale submitted that the insolvency set-off mechanism had replaced all claims and cross-claims under the Contract with a single claim to the net balance, which was not a claim under the Contract but under Bresco's insolvency. One of Lonsdale's arguments in advancing this line of reasoning was the "single dispute" rule, based upon the limited scope within adjudication for the determination of cross-claims. According to Lonsdale, either there was a single dispute about the net balance (in which case it did not arise under the contract), or there were multiple disputes arising by way of various cross-claims. If these cross-claims survived, they needed to be resolved on the taking of a single account, which could not fall within the adjudicator's jurisdiction because of the single dispute rule.

Lord Briggs considered this argument to be misconceived, noting that what is considered to be a "single dispute" within the rule was by no means straightforward. He referred to the case of *Witney Town Council v Beam Construction (Cheltenham) Ltd*[2] *as* providing the most comprehensive judicial analysis of the rule and applying Mr Justice Akenhead's reasoning in that case, Lord Briggs held that a dispute about a cross-claim relied on as a set-off by way of defence to the claim will be part of the dispute raised by the reference. This is because the claim cannot be decided without consideration of the cross-claim by way of defence. Lord Briggs further commented that the single dispute rule would only advance Londsale's jurisdiction argument if the insolvency rules required a liquidator to refer all disputes for claims and cross-claims for set-off to be resolved in a single proceeding. On this point, it was observed that a liquidator may untangle a number of complex disputes to be resolved separately by adjudication, arbitration, the court or other forms of ADR.

Accordingly, the judge held that the existence of a cross-claim operating by way of insolvency set-off did not mean that the underlying disputes about the company's claim under the construction contract would simply "melt away so as to render them incapable of adjudication". Lord Briggs noted that, on Lonsdale's argument, a large claim under a construction contract when combined with a much smaller undisputed cross-claim would trigger insolvency set-off and deprive the adjudicator of jurisdiction, even if, in reality, the only dispute was as to the merits of the larger claim. As Lord Briggs noted, this would be a "*triumph of technicality over substance*".

In addition, Lord Briggs agreed with the Court of Appeal's reasoning that if a liquidator was entitled to pursue a company's claims by arbitration, the same must apply to adjudication. There was no reason why these forms of dispute resolution should be treated differently. Lonsdale's cross-appeal on jurisdiction was dismissed.

Futility

As to arguments of futility, whilst having respect for the Court of Appeal's observations on the subject, Lord Briggs was unable to accept that they afford any proper basis for the grant of an injunction to restrain the pursuit of adjudication merely because the referring party was in insolvent liquidation.

> "There was no basis to conclude that the adjudication regime is incompatible with the insolvency process."

In light of its findings on jurisdiction, the Supreme Court noted that a party has both a statutory and contractual right to adjudication, even where the dispute relates to a claim that is affected by insolvency set-off. It would ordinarily be inappropriate for the court to interfere with the exercise of that right and this should only be done in very exceptional circumstances, which did not apply on the facts of this case.

Lord Briggs observed that whilst one of the purposes of adjudication under the Act is to resolve issues concerning cash flow by enabling a party to obtain summary enforcement of a right to interim payment, this is not its sole objective. Adjudication is also, as was always intended, a mainstream dispute resolution mechanism in its own right, leading to the speedy, cost effective and final resolution of most of the many disputes referred. That was an end in its own right, even where summary enforcement was inappropriate or unavailable.

Further, there was no basis to conclude that the adjudication regime is incompatible with the insolvency process, or with the requirement to deal with cross-claims in insolvency by way of set-off. On this point, Lord Briggs noted that the proof of debt by way of insolvency shares many attractive features with that of adjudication – namely speed, simplicity, proportionality and economy.

Lord Briggs also rejected arguments raised as to wasted costs, and the burden placed on the courts by a supposedly futile adjudication, noting that costs neutrality was built into the adjudication regime for good reason, contributing to its success. And whilst he acknowledged that the joint and several liability to pay the adjudicator's costs was not risk-free, Lord Briggs commented that an insolvent company's liability to make such payment would be an expense of the insolvency, which should provide reasonable reassurance to a respondent.

The appeal was therefore allowed, and the injunction discharged.

CONCLUSION

"Where there remains a real risk that summary enforcement of an adjudication decision will deprive the respondent of its right to have recourse to the insolvent party's claim as security for its cross-claim, then courts will be astute to refuse summary judgment."

In current circumstances, where economic pressures resulting from the COVID-19 pandemic are expected to lead to significant strain on the construction industry and high levels of corporate insolvency, the Supreme Court's decision in *Bresco* provides a helpful confirmation that the insolvency regime and the statutory adjudication regime are not inconsistent, and that a claim by or against an insolvent party can be referred to adjudication, notwithstanding the existence of a cross-claim.

The Supreme Court's emphasis on the fact that adjudication is more than simply a mechanism to assist with cash-flow, and also operates as a standalone dispute resolution mechanism, is also an important reminder to parties to construction contracts of the considerable benefits offered by this cost effective and rapid means of obtaining a decision in relation to legal issues that can arise both during the life of a construction contract, and beyond.

However, parties to construction contracts should also note that whilst the Supreme Court did not consider that the difficulties faced by an insolvent entity of enforcing an adjudication award in its favour could justify an injunction, that does not mean that enforcement by an insolvent party will be rendered any easier. Pursuant to *Bouygues UK Ltd v Dahl-Jensen UK Ltd*[3] and *Wimbledon Construction Co 2000 Ltd v Vago*[4], an insolvent party will still need to persuade a court that "exceptional circumstances" would justify an order for summary judgment to enforce the award, and that there should not be a stay of execution. Indeed, as Lord Briggs noted, where there remains a real risk that summary enforcement of an adjudication decision will deprive the respondent of its right to have recourse to the insolvent party's claim as security for its cross-claim, then courts will be astute to refuse summary judgment.

[1] [2020] UKSC 25

[2] [2011] EWHC 2332 (TCC).

[3] [2000] EWCA Civ 507

[4] [2005] EWHC 1086 (TCC).

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