Insolvent companies and adjudication; the challenges faced at the enforcement stage

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Introduction

The Supreme Court decision of *Bresco Electrical Services Ltd (In Liquidation) v Michael J Lonsdale (Electrical) Ltd* [2020] UKSC 25, has made clear that adjudication by an insolvent company is possible albeit not without certain conditions that would allow the adjudicator's decision to be enforceable.

The recent cases of *Styles & Wood Ltd v GE CIF Trustees* [2020] EWHC 2694 (TCC) and *John Doyle Construction Ltd v Erith Contractors Ltd* [2020] EWHC 2451 (TCC) in respect of summary judgement applications to enforce the adjudicators' decisions, show two sides of the same coin; in the first, the enforcement was granted on the condition that the necessary undertakings were provided, whilst in the second, the enforcement was refused on the grounds of insufficient security.

The principles set out in the Bresco decision and what insolvency practitioners and their agents need to be mindful of when commencing adjudication proceedings, are discussed below.

The Bresco decision

Bresco Electrical Services Ltd ("Bresco") agreed to perform electrical installation works for Michael j Lonsdale (Electrical) Ltd ("Lonsdale") by a sub-sub-contract dated 21 August 2014. Bresco went into CVL in March 2015 and both parties raised claims for damages against each other in late 2017.

Bresco, acting by its liquidator, commenced adjudication in June 2018 and Lonsdale subsequently challenged the adjudicator's jurisdiction on the grounds of the automatic set-off of cross-claims between a company in liquidation and each of its creditors which gives rise to a single net balance between them, as provided for under the Insolvency Act 1986 rules (now rule 14.25 of the Insolvency (England and Wales) Rules 2016). Lonsdale issued proceedings in the TCC for a declaration that the adjudicator lacked jurisdiction and for an injunction restraining the continuance of the adjudication. The judgement was in favour of Lonsdale and Bresco appealed, succeeding on jurisdiction but failing in respect of the injunction; the Court of Appeal held that even if there is jurisdiction, the adjudication, in the context of insolvency set-off, will lead to an unenforceable decision and will therefore constitute an "exercise in futility".

The Supreme Court, reversing the first instance and Court of Appeal decisions, held that construction adjudication is not incompatible with the insolvency regime (as set out under Rule 14.25 of the Insolvency Rules) and in terms of enforcement is not an exercise in futility; the existence of cross-claims falling within the insolvency set-off cannot constitute a basis for denying to a company the right to refer disputes to adjudication, which was conferred by section 108 of the Housing Grants, Construction and Regeneration Act 1996.

However, Lord Briggs, in paragraph 67 of his speech, acknowledged that the challenges of enforcement can be dealt with at the enforcement stage, if there is one, and referred to the discussion of undertakings in the case of *Meadowside Building Developments Ltd v 12-18 Hill Street Management Co Ltd* [2019] EWHC 2651 (TCC). He stated that where there remains a real risk that the summary enforcement of an adjudication decision will deprive the respondent of its right to have recourse to the company's (in liquidation) claim as security for its cross-claim "…*the court will be astute to refuse summary judgement*."

The undertakings as set out in the Meadowside decision

Meadowside Building Developments Ltd ("Meadowside") applied for summary judgement to enforce a decision by an adjudicator dated 3 April 2018. Meadowside was already in liquidation since 2015 and was represented by the liquidator's agent. The Defendant (responding party at the time of the adjudication), 12-18 Hill Street Management Company Ltd ("HSMC") wrote to Meadowside summarising its cross-claims under the Contract, reserving its right to seek declaratory relief from the TCC, and further reserving its position in respect of the adjudicator's jurisdiction on the grounds of "*incompatibility of adjudication in the context of liquidation*". Although HSMC did not take part in the adjudication process, the adjudicator treated the contents of HSMC's letter to Meadowside to which he was copied, as its response to the referral and decided that the amount of £26,629.63 was due to Meadowside.

The Court, although it refused the application, it held that, considering exceptional circumstances for the case, if sufficient financial safeguards were in place the decision of the adjudicator could be enforced.

The satisfactory security should be provided in respect of

- the awarded and enforced sum, so that it is repayable to the responding party should the latter successfully overturns the adjudicator's decision in subsequent tribunal (arbitration or litigation) within a reasonable time; and

- any adverse order for costs made against the company in liquidation in favour of the responding party, for both the potential unsuccessful application for enforcement and any subsequent tribunal in which the responding party would seek to overturn the adjudicator's decision.

In paragraph 87 (3) of the decision, Mr Adam Constable QC outlined what combination of solutions might be appropriate as security by the liquidator:

(a) the liquidator undertaking to the court to ringfence the sum enforced so that it is not available for distribution for the relevant duration;

(b) a third party providing a guarantee or a bond;

(c) ATE insurance.

The rationale behind these requirements could be summarised in paragraph 55 of the decision:

"…in circumstances where there is a satisfactory guarantee in relation to any sum awarded, and/or in circumstances where the sum is temporarily ringfenced pending its becoming finally due in either further proceedings or as a result of the responding party choosing within a period of time not to seek to overturn the adjudicator's decision, the mischief which is at the heart of the justification for not enforcing is eliminated. The responding party retains the security for its cross-claim. Even where there is no cross-claim, it seems to me such security is likely to be needed to permit a company in liquidation to enforce…"

Undertakings provided; successful enforcement (Styles & Wood decision)

Styles and Wood Limited ("S&W") went into administration on 28 February 2020, just after it commenced adjudication proceedings against GE CIF Trustees ("GECIF") on 14 February 2020. The adjudicator notified his decision on 9 April 2020 that S&W was entitled to a sum of just under £700,000 plus VAT and interest. S&W applied for a summary judgement to enforce the adjudicator's decision as GECIF refused to comply on the grounds of "futility".

HHJ Parfitt referred to Lord Briggs's comments in paragraph 67 of his speech in Bresco with regards to the challenges of enforcement as stated hereabove, and emphasised the fact that the administrators had offered undertakings, the suitability of which was the determinative issue of the decision. He then cited the relevant parts of the Meadowside decision and in particular the requirements stated in paragraph 87 of the same.

Finally, he referred to the case of *Balfour Beatty Civil Engineering Ltd v Astec Products Ltd (in liquidation)* [2020] EWHC 796 (TCC), where Mr Justice Waksman applying the Meadowside principles, decided not to grant an injunction sought by Balfour Beaty to

restrain three adjudications (the first was already instigated by Astec and the other two were pending the submission of the notices of adjudication), on certain conditions which, among others, included security for adjudication fees and for adverse costs order against Astec up to £750,000 (£250,000 for each adjudication and subject to Balfour Beatty seeking further security from the court if it should appear that the amount was insufficient).

In the S&W case, the court, based on the particular facts and evidence, granted summary judgement to enforce the adjudicator's decision on conditions as follows:

- The sum decided by the adjudicator would be paid over and ring-fenced as offered by Astec, but the ring-fencing would continue until the conclusion of any appeal process.

- ATE insurance policy would be provided, as amended, at the level of £200,000.

- Both parties were permitted to apply to the same court in relation to any variation of those conditions; that would cover the potential requirement for security of additional costs pertaining to the appeal process (the court considered those costs too remote to be provided for at that stage).

The flip side; enforcement refused due to insufficient undertakings (John Doyle decision)

John Doyle Construction Ltd ("JDC") applied for a summary judgement to enforce an adjudicator's decision made back in January 2018 against Erith Contractors Ltd ("Erith") for the sum of £1.2m approximately. JDC, which entered CVL in June 2013, commenced the adjudication in relation to the disputed final account for landscaping works performed for Erith before the 2012 Olympic Games.

Although the hearing for the contested summary judgement was set down for 17 June 2020, it was postponed so that both parties and the court could take account of the Bresco Supreme Court decision which, coincidentally, was handed down the same date; the case was adjourned to be heard on 2 July 2020. Mr Justice Fraser considered that the quality of the security provided by JDC's liquidator (through its agent) was not sufficient, notwithstanding other observations in relation to the agreement between the liquidator and its agent. In particular,

- JDC did not provide a letter of credit, but rather a letter of intent by the bank (agreeing to issue a letter of credit upon application and receipt of the decision amount) which in the court's view did not represent the proffering of security;

- one of the requirements of the letter of intent was contrary to the ATE policy and potentially contrary to a future grant of a letter of credit by the bank; and

- the ATE policy contained clauses and exclusions that could enable, in certain circumstances, avoidance of cover for an adverse costs order made against JDC.

The judge's conclusions for the security available by way of letter of intent and ATE insurance policy are summarised in paragraph 115 of the decision, where he states:

"I do not consider that the security offered is adequate to meet the legitimate concerns that arise given JDC is in liquidation, nor can the security be properly described as providing (to use the assertion in JDC's skeleton argument) "reasonable assurances to the Defendant that, should it successfully overturn the adjudicator's Decision in later proceedings, the Claimant will be able to (i) repay the capital sum and (ii) meet any adverse costs orders". I reject that characterisation of the security on the facts. I do not consider that the security provides sufficient safeguards to place Erith in a similar position to that which it would occupy were JDC to be solvent."

The court, deciding that there is a real risk that the summary enforcement of the adjudicator's decision will deprive Erith of its right to have recourse to the JDC's claim as security for its cross-claim, refused summary judgement.

It should be noted that Fraser J, further considered the question of the grant of a stay of execution should the summary judgement had been granted; given the facts and evidence of the case (the two mechanisms of security offered by JDC being insufficient), a stay of execution would be ordered even if JDC were to be entitled to summary judgement.

Conclusion

Insolvency practitioners and their agents, who decide to pursue claims through adjudication given the green light presumed by the Supreme Court decision, should be mindful of a number of challenges that still remain to be overcome. Indeed, adjudication can now proceed and not be restrained due to the insolvent status of the referring party.

However, even if the adjudicator's decision is in favour of the insolvent company, the enforcement could still be challenged and furthermore, the courts, taking into account the facts and evidence of each case, could order a stay of execution having the summary judgement granted. From the cases mentioned hereinabove, it is apparent that one of the critical challenges is the provision of sufficient assurances by the administrator / liquidator or its agent regarding the ring-fencing of the proceeds and any adverse costs order should the opposing party overturn the decision in further proceedings (arbitration or litigation) instigated within a specified by the court period.

It should also be noted that, apart from the undertakings, other factors will also be considered by the courts (such as the nature of the dispute, the mutual dealings between the parties or if it concerns a "smash and grab" type of adjudication) and will generally not allow abuse of the adjudication process which rests on the principle of "pay now, argue later".

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