

BRIEFING

SPV WITHOUT A "P" AND THE NARROW
SCOPE OF THE POWER GENERATION
EXCLUSION
MARCH 2018

- THE ENGLISH COURTS WILL NARROWLY INTERPRET THE DEFINITION OF "EXCLUDED OPERATIONS" IN THE CONSTRUCTION ACT 1996
- PARTIES SHOULD TAKE CARE TO ENSURE THEY HAVE EFFECTIVELY RESERVED THEIR RIGHTS TO CHALLENGE AN ADJUDICATOR'S JURISDICTION



"WHEN ASSESSING WHETHER WORKS UNDER A CONTRACT CONSTITUTE "CONSTRUCTION OPERATIONS" UNDER THE CONSTRUCTION ACT, IT IS ONLY THOSE PARTS OF THE WORKS SPECIFICALLY DESCRIBED AS AN EXCLUDED OPERATION THAT ARE EXCLUDED."

In a judgment which will be of particular interest to those in the energy sector¹, the English High Court has confirmed that, when assessing whether works under a contract constitute "construction operations" under the Housing Grants (Construction and Regeneration) Act 1996 (the "Construction Act"), it is only those parts of the works specifically described as an excluded operation that are excluded. Accordingly, an adjudicator will have jurisdiction in relation to a dispute concerning a hybrid contract which includes such excluded works as assembly installation or demolition of plant and machinery, or erection or demolition of steelwork for the purposes of supporting or providing access to plant or machinery on a site where the primary activity is power generation, provided that the dispute referred to the adjudicator does not itself concern the excluded works.

The decision also reiterates that parties should be careful to reserve their rights to challenge an adjudicator's jurisdiction or risk losing such rights and warns that, where the employer is a special purpose vehicle ("SPV") and is awarded a sum to be paid by the contractor pending resolution of the final account, it may be held that a stay of execution is appropriate to achieve "broad justice" between the parties. Finally, the ousting of the contractual adjudication procedure in this case is a reminder to parties to construction contracts that their bespoke adjudication provisions must adhere strictly to the requirements of the Construction Act.

¹ *Equitix ESI CHP (Wrexham) Ltd v Bester Generation UK Ltd* [2018] EWHC 177 (TCC)

Background

Equitix ESI CHP (Wrexham) Ltd ("Equitix") engaged Bester Generacion UK Ltd ("Bester") to design and build the Wrexham Biomass Fired Energy Generating Plant (the "Project") pursuant to a contract dated 29 April 2016 (the "Contract"). Equitix was an SPV specifically created to act as employer for the Project.

Progress on the Project was very slow and Bester's works never progressed beyond the preparatory stages. As a result, in February 2017 Equitix commenced an adjudication seeking a declaration that Bester was not entitled to an extension of time. The adjudicator found in Equitix's favour and in July 2017 Equitix terminated the Contract and notified Bester that it had elected not to continue with the Project.

Following termination and its election not to continue, Equitix issued an Interim Account, setting out its net loss calculable at that date, requiring that Bester pay approximately £11.6m. Approximately £8m of Equitix's claim was made up of sums previously paid to Bester under the contractual payment regime. A dispute arose in relation to the validity of the termination and the basis for the Interim Account, which Equitix referred to a second adjudication. The same adjudicator again found largely in Equitix's favour and ordered Bester to pay Equitix approximately £9.8m plus almost £5,000 a day by way of interest.

Equitix then commenced a claim in the Technology and Construction Court ("TCC") to enforce the adjudicator's second decision.

Decision

Issue 1 - Where a construction contract includes works that are expressly excluded from the scope of the Construction Act by section 105(2)(c), does that preclude an adjudicator from having jurisdiction to decide disputes relating to parts of the works which do not fall within that exclusion?

Section 104 provides that the Construction Act applies to a "construction contract" which includes agreements for the carrying out of "construction operations". Section 105 defines what is meant by "construction operations" and expressly carves out construction operations that would normally fall into the definition but which relate to certain sectors, including power generation.

The Contract as a whole concerned works relating to power generation. However, the Contract would be best described as a "hybrid contract" because the scope of works included installation of the steam turbine and supporting groundworks, which would be categorised as excluded operations, as well as preparatory works such as site compound set up and the production of drawings, calculations, a business plan and bonds, which would not be excluded. Bester contended that because the overall remit of the Contract included works which were expressly excluded from the scope of the Construction Act the adjudicator had no jurisdiction to hear the second adjudication. It argued that the scope of the overall contract, not the dispute actually referred to adjudication, mattered when deciding whether the Contract concerned construction operations as required by section 104(5).

Coulson J rejected this argument. Applying previous TCC decisions in *North Midland v A E & E Lentjes*², *Cleveland Bridge (UK) Ltd v Whessoe-Volker Stevin Joint Venture*³

"BESTER CONTENDED THAT BECAUSE THE OVERALL REMIT OF THE CONTRACT INCLUDED WORKS WHICH WERE EXPRESSLY EXCLUDED FROM THE SCOPE OF THE CONSTRUCTION ACT THE ADJUDICATOR HAD NO JURISDICTION TO HEAR THE SECOND ADJUDICATION."

² [2009] EWHC 1371 (TCC)

and *Severfield (UK) Ltd v Duro Felguera UK Ltd*,⁴ Coulson J confirmed that for the purpose of jurisdiction what matters is whether some part of the dispute referred to adjudication relates to or arises out of excluded operations as defined by section 105(2). He went on to explain that the second adjudication concerned an Interim Account relating to works completed up to termination and thus the issues in it related to what was done by Bester up to the date of termination. Therefore, in respect of jurisdiction, the key question was whether the works undertaken by Bester up to termination amounted to excluded operations as defined by section 105(2)(c).

Coulson J went on to confirm that the preparatory works undertaken by Bester (preparation of bonds, drawings, calculations and a business plan and the placing of a steam turbine order) must fall within the definition of construction operations in section 105(1)(e). Moreover, given that excavation works had not started and no plant was ever brought to site or installed, the dispute in relation to the Interim Account cannot have related to (narrowly defined) excluded operations. Thus Coulson J concluded that the dispute did not relate to excluded operations and so there could be no issue in relation to the adjudicator's jurisdiction.

Issue 2 - On the facts of this case did Bester properly reserve its right to challenge the adjudicator's jurisdiction and/or did Bester confer ad hoc jurisdiction on the adjudicator?

"PARTIES CANNOT RELY ON A GENERAL RESERVATION OF THEIR POSITION ON JURISDICTION IN RELATION TO ONE ADJUDICATION TO LATER CHALLENGE THE ADJUDICATOR'S DECISION IN A SUBSEQUENT ADJUDICATION."

In light of his finding in relation to Issue 1 Coulson J need not have considered Issue 2. However, in case he was wrong in relation to jurisdiction, he provided useful guidance on whether Bester had validly reserved its right to challenge the adjudicator's jurisdiction and/or whether it had conferred ad hoc jurisdiction on the adjudicator by agreeing to his appointment on his standard terms.

In response to Equitix commencing the first adjudication, Bester had written to the adjudicator reserving its position regarding jurisdiction but had made no reservation in relation to the second adjudication.

Whilst highlighting that the position will be heavily dependent on the facts, Coulson J confirmed that "the court will usually look with disfavour on an unspecified general reservation of the responding party's position on jurisdiction if it thinks that it was worded in that way to try and ensure that all options (including ones not yet even thought of) could be kept open".

In this case, Bester failed to reserve its position as to jurisdiction in respect of the second adjudication in a clear and open way. Indeed its only jurisdictional challenge related to the specific issue of timescales and ambush in the first adjudication. In Coulson J's judgment, parties cannot rely on a general reservation of their position on jurisdiction in relation to one adjudication to later challenge the adjudicator's decision in a subsequent adjudication. Even if arising out of the same contract, related adjudications remain separate and different proceedings and parties must reserve their position in respect of each adjudication each and every time.

Although not deciding the point, Coulson J also expressed the view that it may be correct that absent a simultaneous expression of reservations as to jurisdiction, by

³ [2010] EWHC 1076 (TCC)

⁴ [2015] EWHC 2975 (TCC)

conveying express agreement to proceed on the basis of a proposed adjudicator's terms of appointment a party may be giving a "clear and unqualified acceptance of the adjudicator's jurisdiction".

Issue 3 - Given Equitix was an SPV and the final account had not yet been determined, should Bester be granted a stay of execution in relation to the award requiring it to pay a sum to Equitix?

The second adjudication concerned an amount due to be paid on account by Bester pursuant to Equitix's Interim Account. The Contract also provided for a Net Loss Statement to be issued at an unspecified later date, when Equitix' Actual Net Loss had been calculated. Since it was possible for the Actual Net Loss to be less than the amount awarded in the second adjudication, Equitix may, on some unspecified future date, have to repay sums to Bester.

Bester therefore sought a stay of execution pending the issuing of the Net Loss Statement. It argued that as Equitix was an SPV it was entirely possible that following Bester's payment to Equitix, and before the Actual Net Loss could be agreed, Equitix would be wound up, leaving Bester out of pocket.

"COULSON J CONSIDERED THAT "AS A MATTER OF FAIRNESS AND JUSTICE BETWEEN THE PARTIES" A STAY SHOULD BE AWARDED."

Citing the special circumstances of this case, namely that Equitix was "now an SPV with no P (because it has elected not to continue with the Project)" likely to be wound up at the earliest opportunity, and that the final accounting process could take months or years to be concluded, Coulson J considered that "as a matter of fairness and justice between the parties" a stay should be awarded. It is of particular interest that in deciding the terms of the stay, Coulson J considered that the appropriate test is what "would do broad justice between the parties". Thus he ordered that Bester pay £4.5m to Equitix without qualification, £1m into court and that a general stay should apply to the remainder.

Bespoke Adjudication Provisions

It was agreed between the parties that the bespoke adjudication provisions of the Contract did not meet the requirements of the Construction Act and so should be replaced by the adjudication procedure provided for in the Scheme for Construction Contracts Regulations 1998 (the "Scheme"). To a casual observer the adjudication clauses in the Contract (which Coulson J recited in his judgment) do not appear to fall foul of section 108 of the Construction Act (which requires that contractual adjudication provisions meet certain requirements). However, on closer inspection, the 28 day limit for the adjudicator to issue his decision ran, under the contract, from the date of the notice of adjudication rather than the date of the referral. There was also no provision permitting the adjudicator to correct clerical or typographical errors in his decision (the "Slip Rule").

Such non-compliance with the strict wording of the Construction Act may seem technical and trivial in nature. However, it resulted in the entire bespoke contractual regime being ousted and replaced with the Scheme. This highlights the need for parties to take great care when drafting adjudication provisions and making sure that they fully comply with the requirements of the Construction Act. In this case the bespoke adjudication regime was very similar to the Scheme and so there was very little material effect to it being ousted. However, where parties have included particular or unusual adjudication provisions in their contract the effect of having not

“WHERE PARTIES HAVE INCLUDED PARTICULAR OR UNUSUAL ADJUDICATION PROVISIONS IN THEIR CONTRACT THE EFFECT OF HAVING NOT COMPLIED FULLY WITH THE REQUIREMENTS OF THE CONSTRUCTION ACT MAY MAKE A SIGNIFICANT DIFFERENCE TO ONE OR BOTH OF THE PARTIES.”

complied fully with the requirements of the Construction Act may make a significant difference to one or both of the parties.

It should be borne in mind, as mentioned above, that here the parties were agreed that the contractual provisions were ousted and replaced by the Construction Act. Had he had to decide the issue it is possible that Coulson J may have taken a different view.

Conclusions

In relation to challenges to an adjudicator’s jurisdiction based on the express exclusion of certain operations contained in section 105(2), the approach taken in this case is in line with previous TCC decisions. However, Coulson J’s judgment, which largely reflects the TCC’s reluctance to limit the scope of the Construction Act, highlights just how narrowly the courts will interpret the definition of excluded operations. This will be of particular interest to those involved in the power generation sector. Parties must be aware that just because they are contracting for a project related to power generation does not guarantee that every dispute that arises in respect of that project will be excluded from the scope of the Construction Act.

Further, parties should heed Coulson J’s warnings in this case that they must be very careful to ensure that they have effectively reserved their rights to challenge an adjudicator’s jurisdiction. It may not be enough to make a general reservation of rights as to jurisdiction and it must be made at the outset of every adjudication not just the first in a series. In addition, parties must be careful not to confer ad hoc jurisdiction on the adjudicator, in a situation where they would otherwise have grounds for a challenge, by agreeing to proceed on the adjudicator’s proposed terms of appointment without simultaneously reserving rights as to jurisdiction.

Finally, Coulson J has provided some clarification as to when a stay of execution of an adjudicator’s award may be granted and advocates the use of a ‘broad justice’ test for assessing whether and on what terms such a stay will be granted.

FOR MORE INFORMATION

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