

CONSTRUCTION : BULLETIN

Failure to Provide Performance Bonds & Warranties

What sanction will the courts impose?

Failure by contractors to provide performance security documents and collateral warranties is a common concern for employers. The recent case of *Liberty Mercian Ltd v Cuddy Civil Engineering Ltd and Cuddy Demolition and Dismantling Ltd* demonstrated the remedies which are available when a contractor has breached a contractual obligation to provide a performance bond and procure collateral warranties from a sub-contractor.

Background

This is the second case brought by Liberty Mercian ("Liberty") against Cuddy Civil Engineering ("CCE") and Cuddy Demolition and Dismantling ("CDD"). The first case was a dispute about whether Liberty was in contract with CCE or CDD. Liberty had entered into a contract with CCE for civil engineering works. However, CCE is a dormant company with no assets, so the works were carried out by CDD and payment was made to CDD. Liberty ultimately terminated the contract due to defects. Liberty argued CDD was the correct party to the contract, but the court found that Liberty had clearly intended to contract with CCE. The court also decided CCE were in breach of the contract because they had failed to provide a performance bond in favour of Liberty and two warranties from a sub-contractor in favour of Liberty and another beneficiary.

This case concerned Liberty's claim that CCE should be compelled by the court to provide the missing documentation.

Remedies for breach of contract

Where a party fails to comply with a contractual obligation, the most common remedy is damages. The purpose of an award of damages is to compensate the claimant for his loss by putting him in the position he would

have been in if the contract had been performed properly.

However, damages are not always an adequate remedy for failure to comply with a contractual obligation. In such cases, the court has the power to order specific performance, which means the party in breach is compelled to fulfil his contractual obligation instead of paying damages.

Failure to provide a performance bond

The court held that although it would be easy to calculate an award of damages by reference to the value of the bond which CCE should have provided, in this case damages would not be an adequate remedy for CCE's failure to provide the performance bond because CCE have no assets and it is unlikely they could make payment of any damages awarded. The court decided that specific performance should be ordered instead.

CCE argued that an order for specific performance should not be given because it was impossible for them to secure a performance bond in circumstances where (a) the contract had been terminated and (b) CCE did not have the means of meeting the cost of the bond. CCE said they had approached their usual bondsman and he had concluded, after discussing the issue with his usual bond markets, that no one would be willing to provide a performance bond to a company in this situation.

The court was of the view that CCE had not provided sufficient evidence in support of their claim that obtaining a bond was impossible. CCE could not even tell the court how many bond providers their bondsman had approached when making his enquiries. The court stated that it would only accept that provision of the performance



Hawkswell Kilvington

Solicitors to the
Construction and
Engineering Industries

Hawkswell Kilvington

17 Navigation Court
Calder Park
Wakefield
WF2 7BJ

90 Long Acre
Covent Garden
London
WC2E 9RZ

T: 0844 809 9566
E: enquiries@hklegal.co.uk
W: www.hklegal.co.uk

bond was impossible if CCE provided evidence that they could not provide a bond despite using their best endeavours and carrying out extensive searches.

The court also rejected CCE's arguments about having insufficient funds to provide security to the bond provider. Although CCE and CDD were not connected by way of their company structures, it was clear they had some sort of financial relationship because CCE had contracted with Liberty but allowed CDD to carry out, and be paid for, the works. In addition, CCE's defence in this on-going litigation is being funded by CDD. In these circumstances, the court was of the view that CDD could provide CCE with the funding necessary to provide security for the performance bond.

Failure to provide warranties

The contract required CCE to procure two collateral warranties from a sub-contractor, Quantum (GB) Ltd ("Quantum"); one in favour of Liberty and the other in favour of Waterman Transport and Developments Ltd ("Waterman"). Waterman were entitled to a warranty because they had agreed to take responsibility for the entirety of the design work since neither CCE nor CDD had professional indemnity insurance. However, matters were complicated by the fact that Quantum was a sub-contractor to CDD, rather than CCE, and was also in administration.

Again, the court held that damages were not an adequate remedy for CCE's failure. Bearing in mind that CCE has no assets to satisfy any defects claim, the provision of a warranty backed by professional indemnity insurance from Quantum would be of a substantial benefit to both Liberty and Waterman, even though Quantum's financial position was precarious. Furthermore, the court was not prepared to order CCE to pay damages when there is a good chance CCE would not be able to obtain sufficient funds to make that payment.

CCE argued that the court should not order specific performance because it was impossible for them to procure the warranties. They based this argument on the fact that CCE's solicitors had previously written to Quantum's administrator asking them to provide the warranties and been informed that the

administrator was not prepared to provide them. Furthermore, they had no direct contractual relationship with Quantum (who were sub-contracted to CDD) and therefore could not compel them to provide the warranties.

Again, the court thought CCE had not provided enough evidence that provision of the warranties was impossible. No further steps had been taken by CCE in an attempt to procure the warranties after their initial request was declined. In circumstances where Quantum are subject to a clear contractual obligation to provide the warranties and have no apparent defence to their failure to do so, the court considered that it is possible for CCE to put a great deal more pressure on Quantum. The absence of a contractual relationship between CCE and Quantum does not create a significant barrier to obtaining the warranties because there is obviously a commercial relationship between CCE and CDD and therefore CCE can seek assistance from CDD in putting contractual pressure on Quantum. The judge commented that he would only be persuaded that provision of the warranties was impossible if CCE could demonstrate they have used their best endeavours to try to procure them and have still not had any success.

Conclusion of the case

The court concluded that an order for specific performance will be made in relation to provision of both the performance bond and the warranties unless CCE can produce convincing evidence that they still cannot provide them despite having used best endeavours to do so. The judge stated that if CCE can provide evidence that performance of their obligations is impossible, the court will not compel performance because it would be unreasonable to do so.

Implications

Although it is increasingly common for the provision of bonds, guarantees and warranties to be a condition precedent to payment to all or part of the contract value, the deduction of monies will not necessarily provide the employer with adequate compensation for a failure to provide these types of document. Indeed, in this case, the court said that Liberty's deduction of monies from CDD/CCE for failure to provide the warranties was irrelevant to the making

of an order for specific performance. This case demonstrates the willingness of the courts to compel performance of contractual obligations to provide additional documents and sets a precedent for the making of an order for specific performance where a contractor fails to do so.

Specific performance is not a remedy that is frequently given in construction disputes and in this case it appears CCE's lack of assets played a major factor in the court's preference for specific performance rather than damages. It is possible that a solvent contractor would have a better chance of arguing that damages are an appropriate remedy, at least in relation to failure to provide a performance bond. Calculating damages for failure to provide collateral warranties would be much less straightforward.

Another interesting aspect of this case is the court's insistence that CCE use best endeavours to try to procure the missing documents. In relation to the performance bond, it is fairly clear that CCE will need to approach every possible bond provider and seek written confirmation of their position. However, in relation to the warranty, the extent of CCE's obligations is less clear. How many times will the court expect CCE to write to Quantum demanding provision of the warranties before it accepts that the warranties will not be forthcoming? Will the court expect CCE to try to commence legal action against Quantum for breach of contract, even though Quantum is in administration? No doubt these questions will be answered when the next instalment of this dispute appears in the law reports.

CONTACT DETAILS

Hawkswell Kilvington Limited

17 Navigation Court
Calder Park
Wakefield
WF2 7BJ

90 Long Acre
Covent Garden
London
WC2E 9RZ

T: 0844 809 9566

W: www.hklegal.co.uk

E: enquiries@hklegal.co.uk

This bulletin contains information of general interest about current legal issues, but does not provide legal advice. It is prepared for the general information of our clients and other interested parties. This bulletin should not be relied upon in any specific situation without appropriate legal advice. If you require legal advice on any of the issues raised in this bulletin, please contact one of our specialist construction lawyers.

© Hawkswell Kilvington Limited 2014