

## Construction Law Update

### Carillion Liquidation/Contractor Insolvency

The collapse of Carillion will have a huge impact across the construction industry, with the consequences felt by its staff as well as its employers, partners, and supply chain. It brings insolvency within the construction industry back into stark focus.

There are a host of issues, practical and legal, for affected parties to consider and contend with when a main contractor becomes insolvent. In the following bulletins we have summarised some of those issues.

If your business is affected by the collapse of Carillion (whether you are an existing client or not) and you would like a confidential chat, please don't hesitate to get in touch with any member of our team direct or email [enquiries@hklegal.co.uk](mailto:enquiries@hklegal.co.uk).

#### ISSUES FOR A SUBCONTRACTOR TO CONSIDER

Subcontractors will clearly face difficulties as a result of the insolvency of a main contractor. Those engaged directly by the main contractor are likely to be owed money for subcontract works they have carried out, and the longer the main contractor's payment terms, the more they are likely to be owed.

#### Termination:

The Subcontract will almost certainly contain provisions dealing with main contractor insolvency. Termination may occur automatically but in most instances formal notification will be required. It is vital to ensure that the contractual provisions relating to termination are followed to the letter – any mistakes could be costly.

#### Potential recovery of sums due:

Realistically, any 'claim' against an insolvent main contractor is unlikely to achieve a meaningful recovery; it can be lodged and will then almost certainly be added to a list of other claims along with other unsecured creditors.

Therefore, checks should be made immediately to ensure that there are no alternative options for recovery. These might include performance security (such as bonds) that might be in place or credit insurance. Checks should also be made to ensure compliance with the terms/provisions of any such performance security or credit insurance policy.

#### Payment of Sub-Subcontractors:

To compound matters, it may well be the case that a subcontractor is still obliged to pay a sub-subcontractor (despite not having been paid by the insolvent main contractor). Whilst the Housing Grants Construction and Regeneration Act 1996 (as amended by the Local Democracy, Economic Development and Construction Act 2009) outlaws pay when paid clauses in most circumstances, one exception is in relation to upstream insolvency. Therefore, it is possible (for example) for a subcontractor to legally/properly resist making payments to a sub-subcontractor downstream providing there is such a provision in the contract with that sub-subcontractor.

Furthermore, it is crucial to ensure that any outstanding payment or pay less notices are served on time and in accordance with the contract.

#### Collection of Goods/Materials:

Many subcontractors will have provided goods/materials and services to the main contractor and may have retention of title clauses in their subcontract(s) in relation to those goods/materials. Again, this should be checked and any goods/materials should be identified at the earliest opportunity (particularly those that have not (for example) been incorporated into the works).

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### Potential for being employed direct:

Sometimes the ultimate employer may wish to employ a subcontractor direct to try and keep a project progressing (particularly specialist trades). This may provide the subcontractor with some leverage i.e. obtaining favourable terms to continue their work. Consideration should be given to whether the relevant contract(s) provide/allow for this, and the mechanism for progressing on such a basis.

### Immediate Actions:

- If you are affected by the insolvency of a main contractor you should immediately collate and review all relevant contractual documentation relating to the relevant project(s)/works(s).
- Check any relevant termination provisions contained in that contractual documentation.
- Establish what money has been paid, the work done to date, any outstanding payment(s) and where (for example) retention payments are being held.
- Ensure that any outstanding payment or pay less notices that your company has to issue are served on time and in accordance with the relevant contract(s).
- Check to see whether there is any performance security (such as bonds) that might be in place or credit insurance. If there is, checks should also be made to ensure compliance with the terms/provisions of any such performance security or credit insurance policy.
- Materials, goods and equipment on site should be identified immediately. Title to any materials, goods and equipment on site should be investigated.

### ISSUES FOR AN EMPLOYER TO CONSIDER:

#### Termination:

The building contract will almost certainly contain provisions dealing with contractor insolvency. Termination may occur automatically but in most instances formal notification will be required. It is vital

to ensure that the contractual provisions relating to termination are followed to the letter – any mistakes could be costly.

### Calculation of sums due:

Usually, the building contract will provide a mechanism whereby the Employer may take steps to secure/protect the site and then employ others to carry out and complete the works. A form of 'totting up' exercise will then be undertaken (once the work(s) are complete), showing whether any further sums are due to the contractor or whether sums are in fact due to the Employer.

### Issuing Payment or Pay Less Notices:

Even though the contractor has become insolvent, the Employer should still ensure that any outstanding payment or pay less notices are served on time and in accordance with the relevant contract.

### Performance security:

Realistically, any 'claim' against an insolvent contractor is unlikely to achieve a meaningful recovery, it will be lodged and then almost certainly added to a list of other claims along with other unsecured creditors. Therefore, Employers should check to ensure that there are no alternative options for recovery. The might include performance security (such as bonds) that might be in place (and checks should also be made to ensure compliance with the terms/provisions of any such performance security).

### 'Step-In' Rights:

In limited circumstances 'step-in' rights can be exercised whereby an Employer may be able to directly employ sub-contractors, suppliers or professional consultants previously engaged by the main contractor (there may be a desire to consider going down this route to keep a project progressing). Again, this can and should be checked (along with any payment

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obligations relating to exercising any such step-in rights).

### Defects:

If there are defects in work(s) undertaken by a contractor who has become insolvent, it may be that sub-contractors or members of the professional team have provided collateral warranties directly to the Employer. These should be checked.

### Immediate Actions

- If you are affected by the insolvency of a main contractor you should immediately collate and review all relevant contractual documentation relating to the relevant project(s)/works(s).
- Check any relevant termination provisions contained in that contractual documentation.
- Establish what money has been paid, the work done to date, any outstanding payment(s) and where (for example) retention payments are being held.
- Ensure that any outstanding payment or pay less notices are served on time and in accordance with the relevant contract(s).
- An Employer should ensure that all requisite insurance cover remains in place or alternative cover is obtained.
- Check to see whether there is any performance security (such as bonds) that might be in place. If there is, checks should also be made to ensure compliance with the terms/provisions of any such performance security.

*This article 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 article 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 article, please contact one of our specialist construction lawyers.*

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