ALLEN & OVERY

Recent Developments: Dispute Resolution

What you need to know

Welcome to this edition of Allen & Overy's Recent Developments – 'What you need to know'. The purpose of this alert is to keep you updated on the recent legal developments relevant to your industry, and let you know what it means for you and your business.

A review of the recent cases suggests that it is the simple things, often overlooked, which are the focus of an increasing amount of disputes. For example, Courts have recently fired a few warning shots in the direction of those who think mediation agreements, exclusive jurisdiction clauses and Calderbank offers seem straightforward and uncomplicated.

All this makes for an interesting read, and a chance to make sure you are getting the small things right.

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What you need to know

1 Do you think 'exclusive jurisdiction' clauses are boilerplate provisions that don't need much thought? Have you decided to simply accept what the other party has proposed, rather than fight for something a bit clearer, on the basis it won't make any difference?

The NSW Supreme Court has just considered the meaning of such a clause, which just might keep you up all night thinking about what you should have done…

2 The purpose of mediation is to attempt to settle matters before they go to trial. But what does it actually take to reach a settlement?

The Victorian Supreme Court has recently given a warning that agreements reached at mediation might not be as binding as you think, even if you have shaken hands over it.

3 Think you can bank on a Calderbank offer to secure indemnity costs? It is time to think again.

Parties often exchange Calderbank offers, in the belief that they offer some form of costs protection. However, a recent decision of the Victorian Supreme Court shows that this might not be the case, even if your offer is better than the eventual judgment.

4 Companies usually indemnify their officers in respect of legal proceedings arising from issues within the scope of their role. But what is the position if those legal proceedings relate to criminal charges for which an indemnity can't be given, and when the officer maintains their innocence?

A recent decision of the Victorian Supreme Court sheds some light on whether the company is liable for costs incurred by an officer prior to a verdict being handed down.

5 A scattergun approach to misleading and deceptive conduct claims hits a target – the High Court has clarified the application of the proportionate liability regime to these claims involving financial products.

In doing so, the High Court has explained that it is only the defendants to the misleading and deceptive conduct (1041 CA) claims that can point the finger at each other in an attempt to reduce their liability for those claims, leaving the net wide open for other claims based on the same loss – which are not apportionable.

6 Construction contractors are going through a torrid time, with many finding themselves at or near the point of insolvency. This creates issues not only for those companies, but also for the principals that engage them.

In this context, two recent decisions of the WA Supreme Court have considered how the rights of parties under the insolvency provisions of the Corporations Act, and the security for payment legislation, interact.

7 You have a construction contract. You might also have a dispute. But do you have a payment dispute that arises 'under' a construction contract?

Parties are slowly waking up to the power and scope of security for payment legislation. But the first question always must be – does your dispute fall within the scope of the Act? A recent decision has helped clarify that question.

We hope that you find this edition useful.

Exclusive jurisdiction clauses

'Let's take this outside': Have you set the jurisdiction for your dispute?

It is common for parties to include an 'exclusive jurisdiction clause' in contracts, to seek to define the jurisdiction for any future disputes. A recent decision of the NSW Supreme Court shows that it is important that such clauses are very clearly drafted.

In *AAP Industries Pty Limited v Rehau Pte Limited* [2015] NSWSC 468, McCallum J held that a clause stating '*The agreed place of jurisdiction, irrespective of the amount in dispute, is Singapore*' was not an exclusive jurisdiction clause. Rather, it also allowed claims to be brought in New South Wales. Further and in any event, the clause also did not cover all claims arising under the contract, including (for example) claims of repudiation.

The case contains important lessons on how to draft an exclusive jurisdiction clause that will withstand judicial scrutiny.

Facts

AAP Industries Pty Limited (**AAP**) commenced proceedings in the NSW Supreme Court against Rehau Pte Limited (**Rehau**), a Singaporean company, for the alleged repudiation of a supply arrangement. The Supply Agreement contained a clause that provided: '*The agreed place of jurisdiction, irrespective of the amount in dispute, is Singapore*'.

Rehau filed a notice of motion seeking an order that the service of the statement of claim be set aside and/or the proceedings be permanently stayed, on the grounds that the NSW Supreme Court was an inappropriate forum to hear this dispute.

There were some preliminary points to be determined by the court, namely whether the Supply Agreement was a standalone agreement, or should be interpreted with the assistance of the conditions of purchase that governed subsequent purchases between the parties. This was relevant because the conditions of purchase contained a different, more specific, jurisdiction clause. The judge held that the Supply Agreement was a standalone agreement. Ultimately, the main question for determination was whether the clause set out above was an exclusive jurisdiction clause.

Decision

After considering the clause, McCallum J stated '*In my view, having regard to the matters raised in the written submissions, cl XIII is not to be construed as a promise not to sue in a foreign jurisdiction*.' McCallum J came to this conclusion for the following reasons:

– The clause did not use the word 'exclusive'. An objective interpretation of the clause (particularly when compared to a similar provision in the conditions of purchase) suggested that the parties' failure to use such word was an informed choice that had to be given some effect.

– Further, the clause did not use any other words that suggested an intention of exclusivity. For example, there was no reference to 'any' disputes having to be referred, or that it was mandatory for disputes to be referred to Singapore (which may have been suggested by the use of the word "shall").

– Singapore was not the natural forum for the contract or the dispute, given the numbers of factors connecting them with NSW.

Her Honour therefore concluded that the clause was not an exclusive jurisdiction clause. As the NSW Supreme Court was not an inappropriate forum, the proceedings were not stayed.

Interestingly, her Honour also went on to say that even if the clause was an exclusive jurisdiction clause, she would not have applied the clause to the dispute in the present case. This was because the clause stated that Singapore was the agreed jurisdiction '*irrespective of the amount in dispute*'. Her Honour considered that had it been necessary to determine, she would have found that this phrase suggests the clause was intended to apply to an existing dispute concerning the amount to be paid by Rehau to AAP in respect of a specific purchase order placed with AAP. In particular, the clause was not intended to extend to govern a dispute of the kind pleaded in the statement of claim, namely, a repudiation claim.

This case demonstrates how important it is for parties to carefully consider and draft any exclusive jurisdiction clauses in their contracts. Whilst these clauses are often regarded as 'boilerplate' and not subject to negotiation, this case shows that a lack of attention may lead to unwanted results.

Settlement agreement at mediation

But we shook on it! How not to reach a binding agreement at mediation…

In *Rilgar Nominees Pty Ltd v BHA Holdings Pty Ltd* [2014] VSC 632, the parties to a dispute reached an agreement at mediation and shook hands on it. However, some of the parties sought to avoid the deal, and the Victorian Supreme Court had to consider whether to give effect to the settlement agreement.

Despite the tendency of Courts to encourage resolution of disputes through mediation, Justice Sifris refused to enforce the settlement agreement, because one of the parties was not present (even though it took no active part in the proceedings) and it did not satisfy the express formal requirements of the mediation agreement in place. This decision demonstrates the reluctance of Courts to allow a departure from the clear terms of a written agreement, unless they have been clearly and unequivocally waived by all necessary parties.

This case is a timely reminder that all necessary parties should be involved in mediation and any departure from the agreed terms of a mediation agreement must be effected as a clear and unequivocal variation consented to by all of the parties. Conduct such as a verbal agreement, a handshake or even dot points written on a whiteboard is unlikely to amount to a party waiving their pre-existing contractual rights and obligations. This is particularly the case where a mediation agreement stipulates that any settlement agreement is to be made in writing.

Facts

The plaintiff, Rilgar Nominees Pty Ltd (**Rilgar**), and second, third and fourth defendants were shareholders in the first defendant, BHA Holdings Pty Ltd (**BHA**).

In September 2014, Rilgar commenced proceedings against the defendants for allegedly oppressive conduct contrary to sections 232, 233(1) and 1324 of the *Corporations Act 2001* (Cth). BHA proposed to issue shares to existing shareholders at a price which Rilgar argued was unrealistically low and designed to substantially dilute its shareholding. BHA was joined to the proceedings but took no active part.

The proceedings were the subject of a mediation attended by representatives of Rilgar and the second, third and fourth defendants. BHA did not attend the mediation and was not represented. Prior to the mediation, the parties entered a mediation agreement which provided that any settlement agreement must be in writing and signed by the parties (**Mediation Agreement**).

During the mediation it was suggested that BHA cancel and reissue the shares at a higher price, with Rilgar making a contribution partly as share capital and partly as a loan, with an option to convert the loan to shares. The parties stated that they agreed to this upon the terms which had been recorded on a whiteboard. The parties at the mediation shook hands, took photos of the whiteboard and agreed that a written document would be prepared.

After the mediation a draft agreement was prepared and submitted to BHA. However, BHA rejected this agreement. Rilgar contended that the matters in issue had been resolved and sought an order for specific performance of the settlement agreement. In response the defendants made an application for summary judgment against Rilgar, alleging that the claim had no real prospect of success.

Decision

Justice Sifris held that the 'settlement agreement' made at the mediation was unenforceable. As BHA was a necessary party, an agreement could not be reached in its absence. The doctrine of unanimous assent could not be relied upon.

Further, the Mediation Agreement explicitly stated that a settlement agreement would not be binding unless it was signed and in writing. There was no evidence of any discussion to vary or waive this requirement. Shaking hands and taking a photograph of the whiteboard was found to be entirely consistent with having reached agreement in principle, without dispensing with the formal requirements that had been agreed upon.

Justice Sifris held that clear and unequivocal conduct is required to vary or waive a specific term of a prior agreement. The mediation was a consensual process, governed by the Mediation Agreement. This agreement reflected the parties' objectively determined intention that there would be no settlement without a signed agreement.

These proceedings demonstrate that no settlement agreement should be made in the absence of a necessary party or in contravention of the terms of a mediation agreement. This presents the risk of any agreement reached during a mediation process being unenforceable. If the terms of a mediation agreement are to be departed from, this must be done clearly and unequivocally in order for a court to accept that a waiver or variation of terms have been consented to by the parties to the agreement.

Calderbank offers

When you can't bank on a Calderbank

In *Gill v Gill (No 2)* [2014] VSC 612, the Victorian Supreme Court considered the principles of awarding indemnity costs, in circumstances where *Calderbank* offers are made and rejected.

In this case, a party made 4 *Calderbank* offers over a period of six months, all of which were rejected. The party rejecting the offers then achieved a less favourable result at trial. However, the Court refused to award indemnity costs from the first 3 offers, and reaffirmed that indemnity costs will only be awarded where the rejection of a *Calderbank* offer is unreasonable in the circumstances.

This decision serves to remind parties that refusal of a *Calderbank* offer does not in and of itself give rise to a claim for indemnity costs for the party who made the offer. Rather, unreasonableness must be demonstrated in order to trigger this result. This decision highlights the discretionary nature of indemnity costs and reminds parties that they should not be complacent in thinking that indemnity costs will flow automatically if a *Calderbank* offer is refused.

This decision is also important because it identifies what factors the parties should take into account when preparing their own *Calderbank* offers, to increase the prospect that it will give rise to an order for indemnity costs.

Facts

Mr and Mrs Gill were adversaries in a case concerning breach of trust in the Victorian Magistrates Court. Mrs Gill was awarded $100,000 in damages and $14,383 in interest on 15 March 2013. Mr Gill's application for judicial review of the initial decision was dismissed on 30 May 2014, and costs were left to be determined.

Over the course of the proceedings, Mrs Gill had made 4 *Calderbank* offers:

– The first offer, made on 31 January 2013, was for $150,000 in full settlement of the claim, interest and costs. This offer was open until 4pm on the day it was made. There was no response to this offer.

– The second offer, made on 7 February 2013, was in the same terms as the first, but extended the time for accepting until 12 February. Again there was no response to the offer.

– The third offer, dated 4 July 2013, sought $10,000 for costs, dismissal of the judicial review proceedings, and acceptance of the first instance decision. This offer was open for 11 days, and there was no response.

– The fourth offer was made on 30 July 2013, following an unsuccessful judicial mediation on 29 July 2013, and sought $20,000 in costs (being approximately half of the costs incurred), dismissal of the judicial review proceedings and acceptance of the first instance decision. The offer was open for 2 days, and was rejected by Mr Gill on 1 August 2013.

Ultimately, the first instance decision was upheld, and Mr Gill was liable to pay the full amount of the first instance decision, being $114,383.56 plus costs (in excess of $40,000). Accordingly, Mr Gill would have been in a better position if he had accepted any of the 4 *Calderbank* offers.

Decision

In coming to his decision, Derham AsJ restated the six factors identified in *Hazeldene's Chicken Farm Pty Ltd v Victorian WorkCover Authority (No 2)* (2005) 13 VR 435 as guiding his discretion to award indemnity costs. These were: (1) the stage of the proceeding at which the offer was received, (2) the time allowed to consider the offer, (3) the extent of the compromise offered, (4) the prospect of the offeree's success at the time of the offer, (5) the clarity of the offer and (6) whether the offer foreshadowed an application for indemnity costs if the offer was refused.

However, his Honour emphasised that these were merely matters which the judge could have regard to, and were not mandatory or the only considerations.

Crucially, his Honour reiterated that there is no absolute presumption of indemnity costs if the offeree does not achieve a more favourable outcome in the proceedings. Rather it was for the offeror to show that the refusal of the offer was unreasonable at the time of the refusal.

Derham AsJ found it was not unreasonable for Mr Gill to have not responded to the first three offers, because:

– The first offer was not open for a sufficient time to enable it to be properly considered. It also contained a large volume of confusing and irrelevant contentions and allegations. Further, it merely asserted that Mr Gill's claim would not succeed, and failed to explain why the offer was reasonable and should be accepted. This approach was insufficient at a time when the relative strengths of the parties' cases was uncertain. (Interestingly, the judgment did not address another probem with this offer, which was that it was inclusive of the claim, interest and costs. This makes comparison with the judgment on an apples vs apples basis problematic.)

– The second offer merely extended the time for accepting the first offer. It did not add anything further and did not clarify the relative positions of the parties.

– The third offer stated that the original orders of the first instance decision would stand, and that as such the judicial review proceedings were 'an abuse of process'. His Honour found that assessment to be unwarranted. The offer also asserted that Mr Gill had made false affidavits, and these would be prejudicial to his success in the judicial review hearing. His Honour considered this assertion was also inappropriate, and was only included to intimidate Mr Gill into submission. This meant it was not unreasonable for him to fail to respond to this offer.

However, Derham AsJ accepted it was unreasonable for Mr Gill to reject the fourth offer. This was because the offer occurred at a point in time by which he would have known that his prospects of success were quite low, and that the degree of compromise offered by Mrs Gill was generous. Although the Offer was only open for 2 days, which his Honour observed would ordinarily be an unreasonably short amount of time, the fact that Mr Gill responded to this offer to reject it, indicated that it was a reasonable amount of time to respond. In light of these considerations, Mrs Gill was entitled to indemnity costs from this point.

This case confirms that there is no presumption that the rejection of a *Calderbank* offer will result in an award of indemnity costs. Rather, indemnity costs will only arise if the rejection of the offer is unreasonable in the circumstances. It is instructive to note that in assessing reasonableness the Court stated that the offer showed 'an entrenched intolerance' to the opposing party's arguments and a 'distinctly combative approach to the conduct of the litigation'. The point to be taken is that *Calderbank* offers ought to be written in a balanced and moderate way, seeking to point out, with rational supporting information, why the offer ought to be accepted. Approaching them as a 'dear Judge' letter, rather than an attempt to disparage and pressure the other side, will provide the best prospect of a successful outcome in relation to costs.

Indemnification for criminal trials

We will presume you're innocent; but will we pay your legal costs?

In *Leckenby v Note Printing Australia Limited* [2014] VSC 538, the Victorian Supreme Court found that the CEO was entitled to be immediately indemnified by the company for legal costs he was incurring defending criminal charges. If he was ultimately found guilty then he would be required to repay the costs, but that did not change the fact that the liability of the company arose immediately.

This is an important decision in the context of the current regulatory environment, where individual company officers are coming under intense scrutiny. Both companies and their officers should ensure that they carefully examine the provisions of their relevant indemnities, so they are aware of their rights and obligations.

Facts

The plaintiff (**Leckenby**) was the CEO of the defendant (**NPAL**) from 1998-2004. Leckenby was charged with conspiring to bribe foreign officials to secure contracts for the benefit of NPAL, which (if proved) was a criminal offence.

Leckenby incurred legal costs in defending those proceedings. As those costs would exceed his relevant insurance cover, Leckenby sought an indemnity from NPAL, pursuant to a Deed of Indemnity entered into in 2001. Leckenby sought those costs to be paid on an ongoing basis, throughout the proceedings.

The relevant terms of the indemnity were as follows:

2.2 To the fullest extent permitted by law, NPAL hereby indemnifies the Officer against each and every liability for legal costs and expense the Officer may incur or for which the Officer may become liable in defending an action for a liability incurred as such an officer of NPAL unless such costs and expenses are incurred:

(a) in defending or resisting proceedings in which the Officer is found to have a liability for which he or she could not be indemnified pursuant to clause 2.1;

(b) in defending or resisting criminal proceedings in which the Officer is found guilty;

(c) in defending or resisting proceedings brought by the Australian Securities and Investments Commission or a liquidator for a court order if the grounds for making the order are found by the court to have been established; or

(d) in connection with proceedings for relief to the Officer under the Law in which the court denies the relief.

2.3 If the Officer becomes liable to pay any amount in respect of which the Officer is indemnified under this Deed, NPAL must, subject to clause 6, indemnify the Officer by paying that amount…

2.4 It is not necessary for the Officer to incur expense or make payment before enforcing the Officer's right of indemnity under this Deed…'

NPAL argued that entitlement to any indemnity and the right to payment did not arise unless and until the criminal proceedings (including any appeals) had come to an end and a not guilty verdict achieved.

Decision

Sifris J considered two key aspects: the Deed of Indemnity and the relevant legislation.

The clause of the Deed of Indemnity was a relatively standard provision. His Honour found that, on the objective interpretation of the provision, Leckenby's right to indemnity arose immediately upon the relevant legal costs having been incurred. This conclusion was supported by the fact that the Deed did not deal with interest, which would have been expected had the payment been delayed until the end of the proceedings.

His Honour also considered the relevant provisions of the *Corporations Act 2001* (Cth), namely 199A(3) and 212. These sections prohibit a company from indemnifying an officer for legal costs incurred in defending criminal proceedings in which the officer is found guilty. However, this section does not deal with the right to indemnity in respect of costs incurred prior to a guilty verdict being handed down. The explanatory memorandum to CLERP 1998, which recommended the inclusion of these provisions, stated that a company may be able to give a loan or advance in respect of such legal costs. Then, that loan would either need to be paid back to the company if there was a guilty verdict, or otherwise retained by the officer as an indemnity if found not guilty.

In line with this, his Honour concluded that the prohibition on indemnification in s 199A(3) does not 'bite' prior to the verdict of guilty; and in fact will never have effect if there is a no guilty verdict, or the proceedings are settled or abandoned. In those circumstances, there was no purpose in delaying the indemnification of costs.

This decision means that, subject to the terms of the relevant deed of indemnity, companies may be required to foot the bill for ongoing legal costs incurred by officers of the company, even if those costs are related to proceedings alleging a criminal offence. The company will then only be entitled to recover the amounts paid if a guilty verdict is awarded. The legislation is also consistent with this outcome.

As such, both companies and officers should carefully check the relevant terms of any deed of indemnity, to ensure it reflects their intention in this regard.

Proportionate Liability

Keeping things in proportion: The High Court clarifies the liability confusion

The last fifteen years have seen a significant spike in litigation against financial service providers, and their authorised representatives, for loss arising from negligent or misleading financial advice. In these cases, there are often numerous defendants and it is not uncommon for the plaintiff to chase the defendants with the 'deepest pockets', regardless of the defendants' level of actual culpability. In an attempt to dissuade such action (and avoid an insurance liability crisis in the financial services industry), in 2004 the Federal Government introduced a proportionate liability regime for these claims. The objective of the regime was to apportion liability between wrongdoers, in the case of a breach of s1041H of the *Corporations Act* (which prohibits misleading or deceptive conduct in relation to financial products).

The question, however, quickly became: If a plaintiff alleges numerous causes of action, including a claim under s1041H of the *Corporations Act*, is the whole of the damage apportionable or only the damage attributable to the contravention of s. 1041H? In 2014, within one week, two differently constituted benches of the Full Court of the Federal Court answered this question very differently.

In *Selig v Wealthsure Pty Ltd* [2015] HCA 18, the High Court of Australia unanimously clarified the position in relation to this proportionate liability regime. The High Court ruled that an 'apportionable claim' for the purposes of Div 2A is a claim based upon a contravention of s1041H, and does not extend to claims based upon other causes of action.

This decision does not bode well for the 'deep pocketed' defendants, because clever claimants (or their lawyers) may avoid the operation of the proportionate liability regime by pleading causes of action that are not 'apportionable' claims, even if loss for those claims is identical.

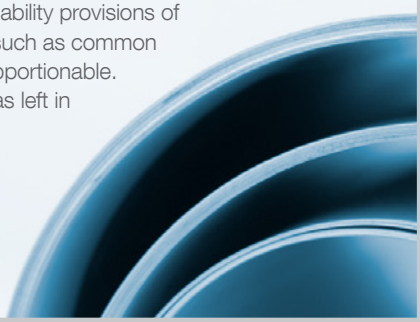
Facts

Mr and Mrs Selig invested in Neovest Limited (**Neovest**) on the advice of Mr Bertram, an authorised representative of the first respondent, Wealthsure Pty Ltd (**Wealthsure**). As it transpired, the Neovest investment was, in effect, a 'Ponzi scheme'. Following the investment, Neovest became insolvent and the Seligs lost their investment and suffered consequential losses. The Seligs commenced proceedings in the Federal Court against numerous defendants, including Wealthsure, Mr Bertram and the directors of Neovest.

Mr and Mrs Selig claimed that the financial advice that they received from Mr Bertram (and Wealthsure) was misleading or deceptive, in contravention of s.1041E and s.1041H of the *Corporations Act*, and the analogous provision in the ASIC Act. They also argued that Wealthsure and Mr Bertram were liable for breach of contract and negligence. Wealthsure and Mr Bertram contended that, by virtue of the proportionate liability regime in the *Corporations Act*, the whole of the loss was apportionable as between them and the other defendants, regardless of whether the loss arose under s.1041H or one of the other causes of action.

The trial judge ordered that the claim arising under s.1041H was apportionable, but that the damage arising from all other claims (including at common law and under other *Corporations Act* sections) was not. Accordingly, the defendants were each 100% liable for the loss not attributable to the contravention of s.1041H. On appeal, the majority of the Full Court of the Federal Court focussed on the nature of the loss or damage suffered rather than the cause of action, and held that all of the claims against the defendants were apportionable, provided that the damage for each claim was in substance the same as the apportionable damage arising from the defendants' contravention of s.1041H. The damages to be paid by Wealthsure and Mr Bertram were reduced accordingly.

The following week, in ABN *Amro Bank v Bathurst Regional Council* [2014] FCAFC 65, a differently constituted Full Court of the Federal Court rejected the decision in *Wealthsure v Selig* and unanimously held that claims that fall outside the specific proportionate liability provisions of the *Corporations Act*, such as common law claims, were not apportionable. Accordingly, the law was left in a state of flux.



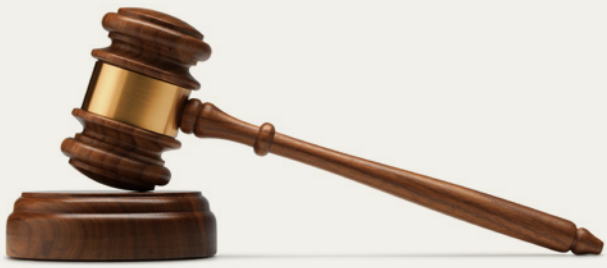
Decision

Mr and Mrs Selig appealed to the High Court.

The High Court unanimously allowed the appeal, and held that an 'apportionable claim' for the purposes of Div 2A is, relevantly, a claim based upon a contravention of only s.1041H. The term does not extend to liability under other heads of claim, and therefore the proportionate liability regime established by Div 2A does not apply to liability arising under other statutory provisions (such as s.1041E of the *Corporations Act*) or common law causes of action (such as negligence). This is the case notwithstanding that the type and quantum of the loss suffered was the same across each.

The High Court rejected the contention that this result would give the regime an unduly limited application. The Court considered that misleading and deceptive conduct takes many forms and may involve a variety of conduct by a number of persons. Accordingly, the Court reasoned, the regime will apply in the number of instances where misleading and deceptive conduct, of different kinds, combine to cause the loss and damage of which the plaintiff complains.

The High Court's decision provides much needed certainty in relation to the application of the proportionate liability regime in the *Corporations Act*. However, the decision will do little to dissuade plaintiffs from pleading multiple causes of action and pursuing the 'deep pocketed' defendants. The decision clearly establishes that the proportionate liability regime can be avoided by pleading alternate claims to the apportionable claims, even where the loss suffered is identical.



Insolvent contractors under the CCA

They are broke – how do I fix this? Paying contractors after they run out of money.

In *Hamersley HMS Pty Ltd v Davis* [2015] WASC 14 and *Hamersley Iron Pty Ltd v James* [2015] WASC 10 (the Hamersley Decisions), Justice Beech has afforded principals working with insolvent contractors some welcome relief given the current economic climate. These actions, between Hamersley and Forge Group Construction, determined that the *Corporations Act 2001* (Cth) s 553C, which allows for a set-off of amounts due between parties where there have been mutual credits, debts or dealings, applies to adjudications made under the *Construction Contracts Act 2004* (WA) (CCA). Furthermore, when there is an off-setting claim from the principal, enforcement of adjudication determinations under s 43 of the CCA should be stayed.

These decisions are a welcome sign that the wider project ramifications that contractor insolvency may have are relevant to the operation of the CCA, and provides a solution to one of the common practical issues faced by principals dealing with insolvent contractors.

Facts

Hamersley (as principal) engaged Forge (as contractor) to perform various works at the Hope Downs 4 Mine project and the Brockman and West Angelas sites. Forge submitted various Payment Claims to Hamersley, which it certified as payable. However, before payment was made, Forge went into external administration. Forge initiated adjudications under the *Construction Contracts Act* (**CCA**) in respect of the outstanding Payment Claims. Hamersley terminated the relevant contracts and, after having recourse to security, responded to the adjudications by claiming that it was exercising its right to set off loss and damage suffered as a result of the Contractor's breaches.

In 2 adjudications, Forge received favourable determinations, and sought leave to enforce. Hamersley asserted that Forge should not be able to enforce where there is a counterclaim that exceeds the sum of the adjudication.

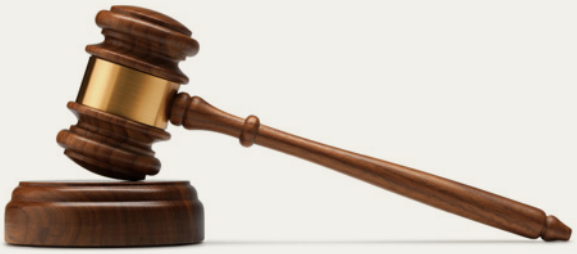
Decision

Beech J considered the application of s 553C of the *Corporations Act* to adjudications under the CCA. In essence, section 553C allows a party responding to a claim by an insolvent company to set-off mutual credits, debts or dealings. Forge argued that s 553C did not apply, because a large part of Hamersley's counterclaim did not exist at the time of insolvency. This was rejected by His Honour, emphasising that s 553C applies to liabilities which were only contingent as at the date of insolvency.

His Honour found that each counterclaim constituted a 'mutual dealing' for the purposes of s 553C of the *Corporations Act*, and that 'the adjudicator was obliged to apply s 553C'. Accordingly, the sum due under the Adjudication should be set off against Hamersley's counterclaim, so that only the balance was payable.

His Honour reiterated that the object of the set-off provisions is 'to do substantial justice between the parties, where a debt is really due from the bankrupt to the debtor to his estate.' In the circumstances, his Honour found Hamersley had established a serious question to be tried as to the counterclaim, and stayed enforcement of the Adjudications, as to grant leave to enforce 'would defeat the purpose and object of s 553C.' Practically speaking, if leave were granted, Forge would receive the full amount of the Adjudicated sum, whereas Hamersley would be left to prove in the liquidation of Forge in respect of its counterclaim. Furthermore, as Forge is under external administration, the policy objectives of the CCA (to maintain cash flow between the contracting parties) were not relevant.

These decisions confirm that adjudicators making determinations under the CCA must consider s 553C of the *Corporations Act*. Practically, this means that a Principal with a counterclaim against an insolvent contractor may only be liable to pay the balance of what is due between the parties, provided the counterclaim is properly substantiated. This reflects an understanding of the wider project ramifications that contractor insolvency may have – and essentially reflects an approach designed 'to do justice between the parties.'



Under a construction contract

What does it mean for a dispute to arise 'under' a construction contract?

An adjudicator only has jurisdiction under the *Construction Contracts Act 2004* (WA) (**CCA**) in respect of 'payment disputes' that arise 'under' a construction contract. In the recent case of *Delmere Holdings Pty Ltd v Green* [2015] WASC 148, Justice Kenneth Martin considered those requirements, and confirmed that they are to be interpreted narrowly. This means that not all claims relating to a construction contract can be heard under the CCA: in particular, rejections of a variation claim, and claims of quantum meruit and unjust enrichment, do not fall within the scope of the legislation. These must be resolved via other processes.

As well as providing guidance on the operation of the CCA, his Honour's decision also serves as a timely caution to those adjudicators who may embark on legal analysis. Whilst his Honour recognised the inherent limitations of the adjudication system, in this case his Honour had no hesitation in describing, in quite colourful language, the failings in the adjudicator's analysis of legal principles.

Facts

Alliance and Delmere were party to a contract, pursuant to which Alliance (as sub-contractor) was to provide piping works to Delmere (as head contractor) at Cape Lambert, WA. In December 2013, Alliance submitted a variation request, in accordance with the relevant regime specified in the contract. Delmere refused the variation.

Alliance asserted that its variation request constituted a 'payment claim' (for the purposes of s 3 of the CCA), and that the rejection of it by Delmere thereby gave rise to a 'payment dispute' (for the purposes of s 6 of the CCA). On this basis, it applied for an adjudication under the Act.

The adjudicator considered that Delmere's rejection of the variation claim constituted a payment dispute, which invoked his jurisdiction. The adjudicator held that Delmere should pay Alliance an amount in the order of $900 000.

Decision

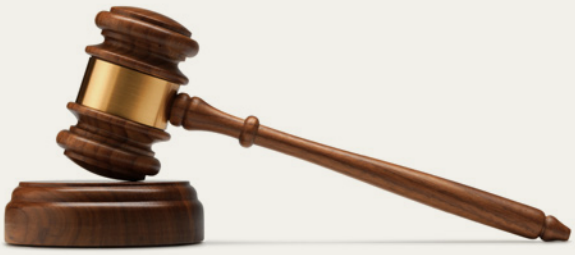
Martin J determined that the adjudicator had made a jurisdictional error, and accordingly quashed the adjudicator's award.

An adjudicator only has jurisdiction under the CCA if there is a 'construction contract', 'payment claim' and a 'payment dispute' in respect of that payment claim. Upon reviewing the relevant provisions, his Honour considered that an actual payment claim, submitted in accordance with the relevant contractual regime, is required. A mere variation claim did not amount to a payment claim, and was not sufficient. His Honour held that the attempt to recast the variation claim as a payment claim was akin to 'applying lipstick to a pig.'

Further, for an adjudicator to have jurisdiction, the payment claim giving rise to a payment dispute must arise 'under' the Act. His Honour considered that the word 'under', as distinct from terminology such as 'in relation to' or 'surrounding', required a narrow construction. In particular, claims such as quantum meruit or unjust enrichment, which were inherent to the variation claim, do not arise 'under a construction contract'. This is consistent with the fact that no payment claim had been invoiced for such claims.

Martin J also criticised the adjudicator's legal reasoning. In particular, he considered the adjudicator's attempts to reason using the legal concepts of unjust enrichment, rights in equity and implied terms as 'incoherent' and 'simply not possible…to reconcile with the current state of Australian law.'

In light of this decision, both contractors and principals should carefully consider whether all jurisdictional requirements have been met, before commencing an adjudication under the CCA. Particular care needs to be taken in relation to claims involving quantum meruit and unjust enrichment, as these appear unlikely to fall within the jurisdiction of an adjudicator.



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