

Claims from Insolvent Contractors

When contractors have been retained to undertake a project but fail to meet the milestones agreed in the contract, it is normal for there to be a procedure by which the contract can be 'determined' (brought to an end).

In a recent case, a council sought to determine the contract of a contractor, which referred the dispute to arbitration to see whether the determination of the contract was lawful. The arbitrator found in favour of the contractor.

The council was concerned that the contractor would seek compensation as a result and that if compensation were paid, it would disappear to the benefit of the contractor's creditors, the contractor being insolvent on a balance sheet basis. It therefore counterclaimed against the contractor and disputed the arbitrator's finding that the determination of the contract was not lawful.

The contractor failed to file a defence to the counterclaim in time, so the council was given judgment. The contractor then applied to have the judgment set aside. The court held that the failure to file a defence in time was an oversight. It also considered that where an insolvent party obtains an adjudication, there is a risk that the court will stay its judgment on the ground of insolvency. In other words, the insolvent party could win, but not be able to enforce the decision. This is likely to apply unless the financial situation of the insolvent party was similar at the time the contract was made, in which case the risk was already present for the other party, or the insolvency was due in significant part to the non-payment by the other party.

In many cases, therefore, a 'victory' by the insolvent party will be a hollow one. However, simply ignoring claims by such companies is unwise. The ability of an insolvent company to pursue such a claim could be attractive to investors who might seek to inject funds into the company for the specific purpose of fighting (and enforcing) the claim.

Contact John Burrowes for advice on any commercial property or landlord and tenant matter.

*For more information contact PCB Solicitors on 01743 248148
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