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ABBEY HEALTHCARE V SIMPLY CONSTRUCT – OPENING THE FLOODGATES OR THE DEATH OF COLLATERAL WARRANTIES

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Rights and wrongs aside, for almost a decade since the *Parkwood decision*, it has been clear that in certain circumstances a *collateral warranty* may be deemed by a court to be a *"construction contract"* for the purposes of the *Construction Act 1996*. This means that the parties will have the right to *adjudicate* at any time under a collateral warranty. As the obligations in a collateral warranty usually only go one way, this means that the beneficiary can adjudicate against the contractor or sub-contractor that provided the warranty.

Parkwood was regarded as *"simply wrong"* by some with fears that it would stop the provision of collateral warranties. However, what happened in practice was that because *Parkwood* primarily focused on the language used, parties who did not wish the Act to apply amended their warranties to remove the offending words and the provision of warranties continued largely undisturbed.

This all came to an end last month when Coulson LJ opened the floodgates to warranty adjudication claims in the Court of Appeal decision in *Abbey Healthcare v Simply Construct*.

This blog takes a look at this judgment and considers the practical implications, with a quick recap of *Parkwood* for context.

PARKWOOD – THE IMPORTANCE OF WARRANTY LANGUAGE

As mentioned above, *Parkwood* was the first case to consider whether a collateral warranty could constitute a "construction contract" for the purposes of the Construction Act 1996.

The essence of *Parkwood* was that, while not every warranty would be a "construction contract", a pointer towards it being so was if the contractor warranted to the beneficiary that it would carry out future construction operations. Whereas the opposite applied if the contractor was simply warranting a past state of affairs as reaching a certain level, quality or standard.

The words "acknowledge" and "undertake" with their forward looking connotations were identified as triggers for the Act's application. Those who did not want the Act to apply to their collateral

warranties sought to stop using these words.

ABBEY HEALTHCARE AT FIRST INSTANCE – THE IMPORTANCE OF TIMING OF EXECUTION VS WHEN THE WORKS WERE CARRIED OUT

After *Parkwood*, the next major judicial consideration of this issue was in 2021 in the first instance case of *Toppan and Abbey Healthcare v Simply Construct*.

As this is the pre-cursor to the Appeal decision, it's worth giving a quick overview of the facts here.

What happened?

In 2015, Sapphire engaged Simply under an amended *JCT DB, 2011 Edition* to carry out the construction of a care home. The contract made provision for collateral warranties to be provided to Toppan and Abbey.

Works commenced in May 2015 and *practical completion* (PC) was certified in October 2016. Simply provided a collateral warranty to Toppan in October 2015 (so pre-PC) and, after protracted wrangling, it provided a collateral warranty to Abbey in October 2020 (so after PC).

Both Toppan and Abbey made adjudication claims against Simply seeking costs for the remediation of fire safety defects.

Toppan adjudication

In the Toppan adjudication the adjudicator awarded Toppan £1,067,247.14. Simply did not pay the sum due and so Toppan commenced proceedings and sought summary judgment to *enforce* the decision. The court ruled in favour of Toppan, ordering Simply to pay the sum awarded by the adjudicator.

Abbey adjudication

The Abbey adjudication proceeded in parallel. Simply took the *jurisdictional objection* that the Abbey collateral warranty was not a construction contract. The adjudicator gave a non-binding ruling on jurisdiction in favour of Abbey and awarded them £908,495.98. Simply refused to pay.

On enforcement, Simply argued that the collateral warranty was not a construction contract under the Construction Act so the adjudicator had no jurisdiction.

First instance decision

At first instance the court held that the Abbey collateral warranty was not a "construction contract".

As the collateral warranty had been executed four years after PC, the conclusion was that there were no "construction operations" left for the contractor to perform. Therefore, it did not make

commercial sense to treat the collateral warranty as a construction contract for the purposes of the Construction Act 1996.

WHAT WAS THE POSITION AFTER PARKWOOD AND ABBEY HEALTHCARE AT FIRST INSTANCE?

Although the *Abbey* first instance decision did not provoke much debate as the collateral warranty did not fall within the Act, our former colleague John Hughes D'Aeth warned in his *blog on this decision*:

> *"… by upholding and perpetuating the distinction based on timing, it reinforced the flawed reasoning underlying Parkwood. As things … stand:*
>
> - *At least some CWs are subject to adjudication, when that was never the purpose behind the Construction Act 1996;*
> - *Whether the Construction Act 1996 applies to a CW will depend heavily on the chance factor of when it is executed; and*
> - *Different rules apply to CWs and TPRs.*
>
> *None of this makes logical sense, and it is going to need the Court of Appeal to sort out the mess…"*

ABBEY HEALTHCARE – THE COURT OF APPEAL'S DECISION

Abbey appealed the decision. The court was asked to determine the following issues:

1. Can a collateral warranty ever be a construction contract as defined by *section 104(1)*?
2. If the answer to Issue 1 was yes, did the terms of the Abbey collateral warranty make it a construction contract as defined by section 104(1)?
3. If the answer to Issue 2 was no, did the date on which the Abbey collateral warranty was executed make any difference?

In a majority decision, with Coulson LJ and Peter Jackson LJ allowing the appeal and Stuart-Smith LJ dissenting, the Court of Appeal ruled that the collateral warranty in question was a construction contract for the purposes of the Construction Act 1996 and so the parties could adjudicate under it.

Key points from the judgment include:

Can a collateral warranty ever be a construction contract as defined by section 104(1)?

Yes, although it will always depend on the wording of the collateral warranty in question.

A document which provides a simple fixed promise or guarantee in respect of a past state of affairs (like a product guarantee) may not be a construction contract. This is because it does not recognise or regulate the ongoing carrying out of any future work.

The court provided the following example wording:

> *"We completed these works two years ago and we warrant that they were completed in all respects in accordance with the Building Regulations…"*

Conversely, a collateral warranty that the contractor was carrying out and would continue to carry out construction operations may well be a construction contract because, unlike a product guarantee, it is a promise which regulates (at least in part) the ongoing carrying out of construction operations.

If the answer to Issue 1 was yes, did the terms of the Abbey collateral warranty make it a construction contract as defined by section 104(1)?

- The standard wording that the collateral warranty used whereby Simply warranted that it "has performed and will continue to perform diligently its obligations under the contract" was a collateral warranty of both past and future performance of the construction operations. It was not a collateral warranty limited to the standard to be achieved; neither was it a collateral warranty limited to a past or fixed situation. It was a warranty as to future performance (regardless of the fact that Simply had completed the works in question four years previously). It was this that differentiated the Abbey collateral warranty from a product guarantee.
- It is also worth noting that the fact that the collateral warranty did not include the *Parkwood* trigger words "acknowledge" or "undertake" held little sway with the court, with Coulson LJ noting that:

> *"… the absence of the word 'undertakes' in the present case makes [no]…material difference: indeed, I regard any difference between 'warrant' and 'undertakes', in the present context, as hair-splitting…"*

If the answer to Issue 2 was no, did the date on which the Abbey collateral warranty was executed make any difference?

No – in a nutshell, because the collateral warranty contained future-facing obligations and was retrospective in effect, the date of execution was irrelevant. In this case, it would have led to two collateral warranties, in exactly the same terms, but signed at different times, being treated differently. "**That would make for commercial absurdity.**"

PRACTICAL IMPACT

The collateral warranty in *Abbey* contained market standard wording and the court made clear that unless collateral warranties evolve to be as sparsely worded as product guarantees, then clever drafting alone will not exempt a collateral warranty from the scope of the Construction Act 1996. In each case, whether the Act applies will be a question of fact but most standard collateral warranties will now be caught.

Therefore, bar a Supreme Court judgment that overturns this decision, this case could open the floodgates to adjudication claims under collateral warranties.

Even if a court ultimately construes that the collateral warranty in question is not a construction contract for the purposes of the Act, this is unlikely to stop parties launching adjudications in the first place. And, of course, the parties cannot contract out of the right to adjudicate.

So what does this mean for parties in practice?

- For those who provide collateral warranties, if you continue to provide collateral warranties then you need to be aware that you could face adjudication claims under them, regardless of whether a court may ultimately determine that the Act applies. This gives you two options:
  - accept adjudication applies and consider whether you wish the *Scheme for Construction Contracts 1998* to apply to the collateral warranty or whether you want to include express wording to align the adjudication rules with the main contract;
  - to avoid adjudication, offer *third party rights* (TPRs) instead.
- For beneficiaries of warranties clearly this decision is good news as it widens the scope of recourse under collateral warranties to include adjudication.
- For employers, the headache may come if contractors, consultants and sub-contractors refuse to provide collateral warranties. As mentioned above, there is a simple solution to this: TPRs.

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MEET THE TEAM

Gareth Stringer

London

gareth.stringer@bclplaw.com
+44 (0) 20 3400 4761
