Russell McVeagh

Breaking Ground

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Industry spotlight

Supply chain delays in the construction industry

The results of the 2020 Russell McVeagh Construction Survey highlighted an industry concern of supply chain disruption to come, in light of the continuing effects of COVID-19 internationally. This concern has proved to be well-founded, with delays in the supply of construction materials throughout New Zealand over recent months, and significant backlogs seen at the ports.

It is important for those involved in construction projects to understand which contractual terms under NZS 3910:2013 and similarly worded contracts may be relevant, and how parties could address such issues when they arise.[1]

Extensions of time

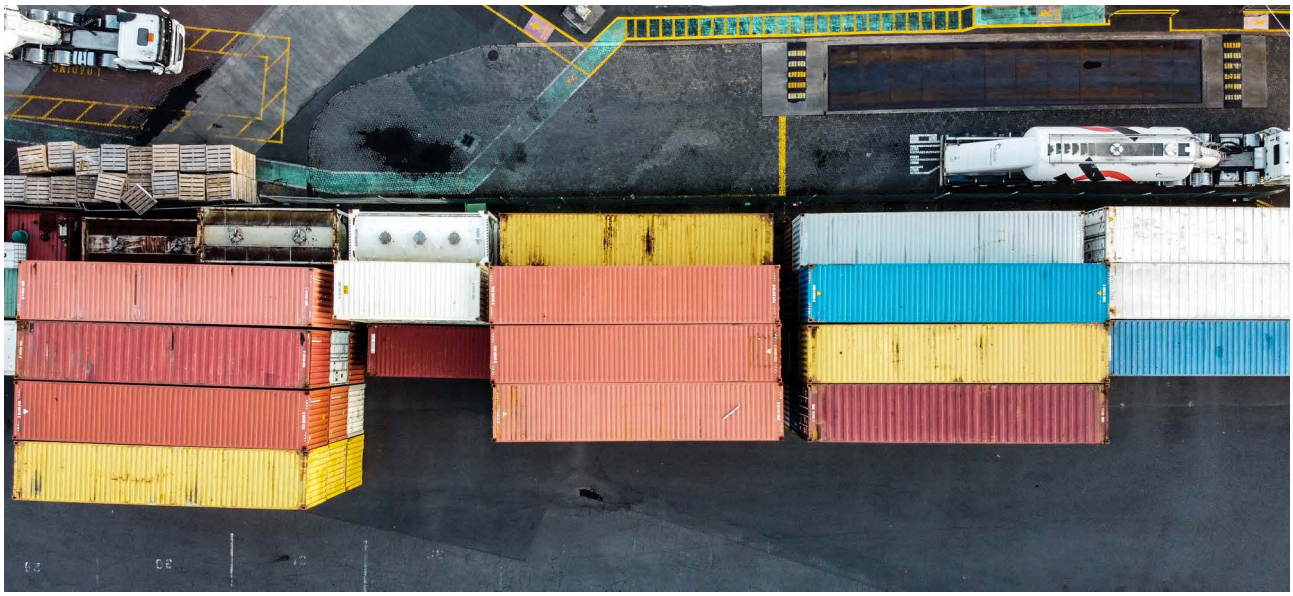
Where supply of materials is delayed, a contractor may seek an extension of time. A number of qualifying events might be relied on:

The delay was not reasonably foreseeable (cl 10.3.1(f)).
This is the most obvious claim a contractor might make. The extent to which this clause applies will depend upon the exact reason for the delay and what was foreseeable when the contract was tendered for. If the cause of delay relates to COVID-19, and tendering for the contract occurred during 2020, it will be important to be clear on exactly what was (or should have been) understood about COVID-19 and its likely ramifications at that time. There are timelines of key events available online which may be useful in assessing this.[2]

When establishing what was reasonably foreseeable, it can be useful to draw from the law of negligence, where 'reasonable foreseeability' is a key concept in determining the scope of damage for which a defendant may be liable. In that context, a foreseeable risk is a "real risk", being "one which would occur to the mind of a reasonable man in the position of the [defendant] and which he would not brush aside as far-fetched."[3] One might therefore ask: is this a risk a competent contractor might have priced for? If so, cl 10.3.1(f) is unlikely to apply.

If it is established that cl 10.3.1(f) does apply, the contractor would be entitled to time, but not to time-related costs (cl 10.3.6).

The net effect of any Variation (cl 10.3.1(a)).
There are a number of ways this clause might be relied upon. For example, if the goods were ordered to perform extra work requested by the Principal, the delay might be said to be part of the "net effect" of that Variation. If they were ordered



following the late issue by the Engineer or Principal of any instruction, documents or Drawings, a similar argument might be made (cl 2.7.7). In some circumstances, where the delay relates to a nominated subcontractor supplier, this may also lead to it being considered as the net effect of a Variation (cl 4.2.6). Such delays would entitle the contractor to both time and to time-related costs (cl 10.3.6).

Other possibilities.
There are other clauses which might be said to apply, depending on the precise facts. For example, in some cases the delay might be said to be due to a "Default of the Principal" (cl 10.3.1(g)), or the result of a new statute, regulation or bylaw (cl 5.11.10). Manufacturing delays or delays due to port backlog, however, are unlikely to trigger these provisions.

In each case, if the delay in supply continues, the contractor may need to give more than one notice (cl 10.3.3).

If the delays could have been avoided, the Engineer may take the view that an extension of time is not one to which the contractor is "fairly entitled" (cl 10.3.1). The parties' ability to reduce the impact of the delay in provision of those particular materials should therefore be carefully considered. Have sufficient investigations been made as to whether there could be an alternative source for the materials? Is there another, more readily available, material which the parties can agree is suitable for substitution?

Sometimes there may be no applicable clause under which a contractor can seek an extension of time. In those cases, it will simply fall to the contractor to bear the burden of the delay.

Frustration of contract (cl 14.1)

If the delay is considerable, and the relevant materials critical to performance of the contract, a party might claim that the contract has become impossible of performance, and therefore "frustrated" under cl 14.1. Alleging frustration, and seeking to terminate a contract, are significant steps and should not be taken without first seeking legal advice.

Tendering practice now

The possibility of supply chain delays is one of many risks that parties should now always consider at the time of tendering for a new project. Parties may wish to explicitly discuss and agree upon a process to be followed in the event of specified delays. One possibility is adding a substitution clause to their contract, by which the parties agree, in the event materials are unavailable or their supply considerably delayed, through no fault of either party, certain substitutions will be permissible.

Contributors:

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Footnotes

1 Clauses set out here refer to NZS 3910:2013. Similar clauses appear in other NZS contracts.
2 For the World Health Organization's timeline of key events see here; for the New Zealand government's timeline of New Zealand-specific events see here.
3 *Overseas Tankship (UK) Ltd v The Miller Steamship Co Pty Ltd (The Wagon Mound (No 2))* [1967] 1 AC 617 (PC) at 643, adopted in New Zealand in *Wilson & Horton Ltd v Attorney-General* [1997] 2 NZLR 513 (CA) at 520.

Case Law Update

New Zealand

Rebnik Properties Ltd v Dobbs [2020] NZHC 3494

Released shortly before Christmas, a High Court decision has confirmed that a party contracting as an agent for another will be personally liable if they do not identify their principal before the contract is entered. It also sets out the means by which the sum payable under a construction contract will be calculated where the contract terms are not sufficiently clear on price.

Background

Mr Dobbs carried out extensive remedial construction work at Mr Ring's house. The contract between them was informal, arising from a combination of email correspondence, conversations, and conduct. The contract did not specify a price, or a pricing mechanism, though hourly rates for some types of labour were sometimes recorded in emails.

The relationship soured. Mr Ring thought that he had been overcharged. Mr Ring's assignee, Rebnik Properties Ltd (Rebnik), brought proceedings against Mr Dobbs and, in the alternative, his company, Aluminium Repairs Ltd (ARL). It claimed that it was an implied term of the contract that Mr Ring would be charged only what was "reasonable", and this term had been breached. Mr Dobbs/ARL argued that the correspondence between the parties as to hourly rates amounted to agreement on price, and there was no need to imply any such term into the contract.

Mr Dobbs also claimed to have undertaken all work on behalf of ARL. He said that, to the extent there was any liability, it was for ARL alone to bear. ARL and Mr Dobbs separately brought proceedings against Mr Ring, seeking payment for two final invoices.

The key issues for the Court were therefore:

- Who was liable to Rebnik: Mr Dobbs or ARL?
- Was it an implied term of the contract that Mr Dobbs/ARL would charge Mr Ring only a reasonable price for the work?
- If so, what was reasonable?

Outcome

In the High Court, Campbell J held:

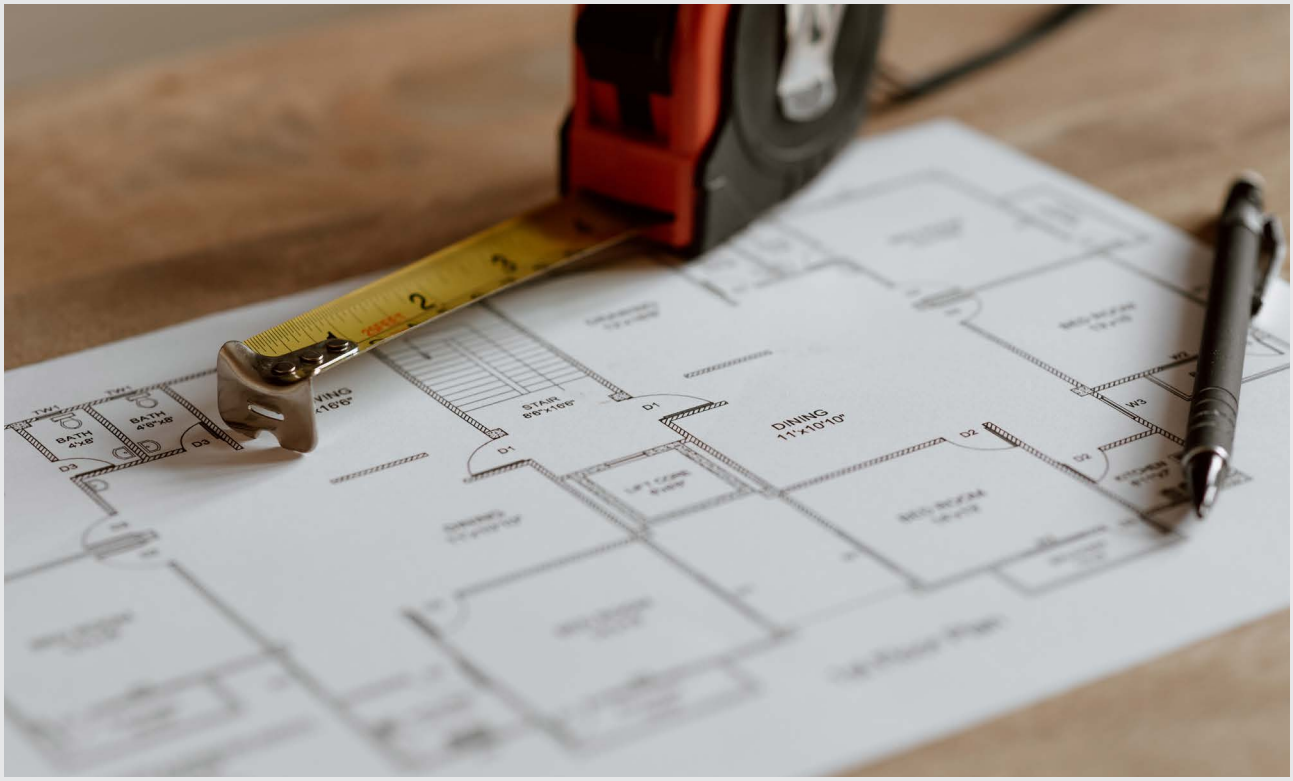
Liable party

- If an agent acts for an undisclosed principal, the agent will be liable.
- The onus is on the agent to disclose to the other party that they are acting in that capacity. They must do so clearly, and prior to or at the time of entry into any contract. This was a clear restatement of the law as it was understood to be.
- On the facts, no disclosure regarding agency had been made by Mr Dobbs to Mr Ring. At the time of their first dealings, ARL had not been incorporated. Mr Dobbs gave every objective indication to Mr Ring that he was acting on his own account, including sending an invoice that used a trade name not a company name, using an email address that appeared to be a personal one, signing off his emails simply as "Troy", and requesting that payment be made into a bank account which was in his own name.
- To the extent there was any liability, it was therefore to be borne by Mr Dobbs personally.

Reasonable price

- In some circumstances, absence of a price provision in a contract may be taken to mean that the parties have not concluded their agreement, and there is no binding contract at all. Here, both parties accepted there was a binding contract.
- The correspondence between the parties as to hourly rates was not sufficient to amount to agreement on those rates. Even had such agreement existed, the contract would still have been insufficiently clear as to the overall price, which was to cover both labour and materials.
- Where a construction contract is silent as to price, a term will generally be implied that the contractor is entitled to be paid only a "reasonable" price. The contract here was subject to such a term.

Justice Campbell then assessed what constituted



a "reasonable" price in the circumstances of this case, including by reference to the conduct of the parties during the project (that is, which party was responsible for various inefficiencies), and the expert opinion evidence given during trial by quantity surveyors. It was determined that a reasonable price was around $800,000 less than Mr Ring had in fact been charged. Rebnik was accordingly able to recover that excess, plus interest, and neither Rebnik nor Mr Ring were required to pay the two remaining invoices.

Takeaways

This case highlights four key points:

- If you, as an individual, are undertaking work on behalf of a company, you should make this clear at the outset. If not, you risk being held personally liable if things go wrong.
- The simplest means of making this clear is ensuring that a written contract is executed, with the relevant parties clearly identified. In the absence of a full written contract, your role as agent should still be specified clearly in writing (for example, in an email).
- Even agreement as to hourly rates will not be sufficient to constitute agreement on price if the contract covers both labour and materials. Where there is no agreement on price, there is a risk that the contract will be held incomplete, and unenforceable.
- Make sure the price, or pricing mechanism, is clear and complete. Whether there is no agreement (such that claims for payment are made on a quantum meruit basis), or the contract is silent as to price (so that a "reasonable sum" is to be paid), there will be inherent uncertainty on the price to be paid.

Contributors:

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Case Law Update

England and Wales

What is the effect of an agreement being "subject to contract"?

A recent decision of the High Court of England and Wales, *Aqua Leisure International Limited v Benchmark Leisure Limited* [2020] EWHC 3511 (TCC) has confirmed that, where parties reach an agreement expressly stated as "subject to contract", that agreement will not be binding until a written contract has been signed.

Background

Benchmark was a site developer, and Aqua Leisure a building contractor. The parties entered into a building contract regarding the development of a waterpark.

Following practical completion, there was a dispute as to how much money was owed to Aqua Leisure. The dispute was referred to adjudication. Following receipt of the adjudication determination, the parties decided to negotiate a settlement agreement. The terms of that agreement were expressed in email correspondence as being "without prejudice and subject to contract".

Benchmark paid some, but not all, of the sum ostensibly agreed. Aqua Leisure provided Benchmark with a contract, and made multiple requests over a period of months that it be signed. Benchmark did not sign it.

Aqua Leisure then commenced court proceedings seeking to enforce the adjudication award. Benchmark argued that the award was no longer enforceable, on the basis it had been overtaken by the parties' negotiated agreement.

Outcome

The Court held:

- The parties had reached agreement, in the sense that there was a "meeting of the minds", during the course of their discussions and correspondence.
- Such agreement would usually be treated as binding. However, here, key emails were expressly written on a "without prejudice and subject to contract" basis. There was no suggestion that the oral agreement reached had been characterised differently. The parties accordingly shared a common understanding that the agreement would not be binding until reduced into writing and signed as a contract.
- As a result, the adjudication award had not been superseded. Benchmark was required to pay the sum under the adjudication award (though excluding certain costs, which the Court considered the adjudicator had not held the power to award).

Analysis

The conclusions of the Queen's Bench were in line with an English Court of Appeal decision regarding a property dispute, determined just a few weeks earlier. In *Joanne Properties Ltd v Moneything Capital Ltd* [2020] EWCA Civ 1541, the Court confirmed that use of the phrase "subject to contract" in negotiations meant that neither party intended to be bound unless and until a formal contract was executed, and that, when negotiations were begun "subject to contract", that condition would be carried through the negotiations to their completion.

It also accords with the position under New Zealand law. Here, the following principles will apply:

- Where the parties have expressly stated that an agreement is "subject to contract", courts will usually draw an inference that the agreement will not be binding until that formal document has been executed.[1]
- In those circumstances, either party is free to withdraw from the arrangement at any time prior to that formal execution.
- Letters of intent will not be sufficient to show an agreed contract. Instead, they are likely to be regarded as confirming that the parties were continuing to negotiate, with the intent that a contract would be concluded in due course.[2]
- In some circumstances, the parties may be taken to have intended not to be bound until after a formal contract was signed,

even in the absence of explicit "subject to contract" wording.[3]
- However, adding the words "subject to contract" only after an agreement already intended to be binding is reached will not alter the fact that a contract has already been formed. [4]

Takeaways

- A binding contract may be made subject to a specified acceptance procedure, or expressed as being subject to certain preconditions ("subject to contract" may be most common, but others, including "subject to Board approval" may also be used). In such cases the agreement will not be binding until that process has been followed and those preconditions met.
- It is important not to lose sight of what you are currently bound to while you are negotiating. Until any subsequent agreement is final and binding it will not supersede that earlier position.
- It is permissible for parties to negotiate an acceptable settlement between themselves after an adjudication determination has been given. However, the determination will be enforceable pending such an agreement. If the parties settle an adjudicated dispute prior to the adjudication determination being given, the adjudicator must terminate the adjudication proceedings. [5]

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Footnotes

1 *Verissimo v Walker* [2006] 1 NZLR 760 (CA).
2 *Electrix Limited v The Fletcher Construction Company Limited* [2020] NZHC 918. For a more complete analysis of this case, see "Assessing sums payable in the absence of a contract: Electrix Limited v The Fletcher Construction Company Limited" by Michael Taylor, Joanna Trezise and Belinda Green, accessible here.
3 This is the usual inference in the case of the sale and purchase of land [*Smada Group Ltd v Miro Farms Ltd* [2007] NZCA 568], an inference reinforced by the Property Law Act 2007 requirement for such an agreement to be recorded in writing in order to be enforceable (Property Law Act 2007, s 24). The inference may also be applied when parties are negotiating a complex business transaction involving large sums of money [*Concorde Enterprises Ltd v Anthony Motors (Hutt) Ltd* [1981] 2 NZLR 385 (CA)].
4 *Croser v Focus Genetics Limited Partnership* (2548500) [2020] NZCA 367.
5 Construction Contracts Act 2002, s 48(5)(a).

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