

Court can act as bondsman and require contractors to procure warranties through specific performance

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We come across situations sometimes where contractors agree to enter into contract with clients, with a form of bond or collateral warranty attached to the contract. The contract is signed and works commence on site. Both the contractor and the client are well into the project. The contractor then fails to procure a bond and fails to procure collateral warranties from its sub-consultants (which were in fact under the contract). The client requests the performance bond from the contractor. The contractor procrastinates and starts negotiating with the client on the form of bond to be used. By this point this has become a commercial issue for the client. The client is now also concerned that the contractor has not procured the collateral warranties from its key designers. The contract is terminated for other reasons.

The *Liberty Mercian Limited v Cuddy Civil Engineering Limited, Cuddy Demolition and Dismantling Limited* cases seek to protect a client in a similar position. There have so far been three cases in total in front of Mr Justice Ramsey between these two parties. In the first two cases, the court found that a contract existed between Cuddy Civil Engineering Limited ('Cuddy') and Liberty Mercian Limited ('Liberty Mercian'). The first case also highlighted the importance of knowing who the contractor is – is it really the contractor undertaking the works or some other entity/group company? In the second case, the court found that Cuddy was in breach of contract for not providing a performance bond and two collateral warranties, and it required Cuddy to use 'best endeavours' to obtain these documents, even though the contract between Cuddy and Liberty Mercian had terminated. The approach taken by Mr Justice Ramsey was not to ratchet up and force Cuddy to provide these documents, but instead he approached the matter in stages, which provided Cuddy an opportunity to take action and remedy the situation.

In the third case, Cuddy and Liberty Mercian provided evidence in relation to Cuddy's efforts to procure a performance bond. The obligation on Cuddy to procure the bond was one of 'best endeavours'. How did Cuddy discharge this? Cuddy consulted underwriters and banks who suggested that a performance bond could not be secured as the works were now nearing practical completion, the NEC3 form of contract would need to be amended to make it acceptable to the underwriters, and that the contentious relationship between Liberty Mercian and Cuddy made these underwriters and banks uneasy. As far as the banks were concerned, each required 100% cash payments or declined to provide a bond outright. There was also the general view that it would not be possible to issue a performance bond guaranteeing performance of a contract which no longer existed and therefore was not capable of being performed. The court considered that Cuddy had complied with its obligation to use best endeavours to secure a performance bond, but sadly it could not, so it would be impossible for the court to order specific performance requiring Cuddy to procure a bond in the terms attached to the contract.

The financial information available on the surety is likely to be quite important – Liberty Mercian explored the possibility of 'Evolution' (a surety) underwriting Cuddy's bond. Cuddy took the view that Evolution, an insurance company based in Gibraltar, was unrated. It requested the court not to require Cuddy to enter into arrangements with such a company especially where a substantial cash deposit was also required to be made. Although the court examined the form of bond proposed by Evolution and considered that if the court wished it could grant specific performance of a bond on revised terms, the much stronger argument related to the financial information available on Evolution, and the contractual provision between Liberty Mercian and Cuddy which required the bond to be placed with a bank or insurer in a strong financial position. The court considered that there was limited financial information on Evolution and a large amount of money £420,000 to which Evolution would have free access. As the company was registered in Gibraltar, the sum could well be placed somewhere outside the UK. If a financially prudent party would not place a bond in such a circumstance, neither was the court going to allow this.

The court therefore considered that substituted performance was the best solution – the sum of £420,000 should be paid into court to stand as equivalent to the performance bond. Liberty Mercian would need to apply to Cuddy to obtain payment. The court further considered that the sum should be paid out to Cuddy if proceedings were not commenced within six months, subject to Liberty Mercian applying for an extension. Therefore whilst Cuddy could not obtain a performance bond in the form attached to the contract, the court took the view that there should be substituted performance in this case by way of a payment into court as an equivalent to the provision of the bond.

The court also dealt with the two collateral warranties that needed to be procured by Cuddy from Quantum (GB) Limited ('Quantum', an insolvent company) – one in favour of Liberty Mercian and the other to Waterman, another entity. Cuddy was required to use 'best endeavours' to procure these warranties. The court considered that there was evidence before the court that up until 21 January 2012 Quantum had professional indemnity insurance organised through a Lloyd's broker with a limit of indemnity of £5,000,000. However, it was unclear whether or not Quantum had current valid insurance cover. The court took the view that if there was no insurance cover then Liberty Mercian and Waterman would not derive any benefit from having a warranty or want to seek to enforce an order for specific performance.

The court considered that, if proceedings were commenced in court against Quantum, the proceedings very likely might not be defended by Quantum but 'points may be taken up by its insurers'. As there was some evidence that the warranty would be backed by insurance, the court considered that specific performance against Cuddy could be granted for its obligation to procure warranties from Quantum.

This case illustrates how the court can step-in to safeguard a client's interest where a contractor has failed to procure and provide documents, which the contractor agreed to provide to the client in the first place, but failed to do so.

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