



Insolvency Issues in Construction
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Introduction

The Construction Industry very exposed to insolvency

- Cyclical
- Low profit; high fixed assets/high cash flow
- Cash flow “pay when/if paid”
- The contractual documentation

Introduction

- As an industry sensitive to prevailing economic conditions
- The 'current' credit crunch has resulted in:
 - Decimation of the residential sector
 - Slow down in public sector projects
 - ❖ Re-negotiation of PPP/PFI
 - ❖ Reduction in the number of infrastructure schemes
 - The 'Political' agenda
 - 'spend to success, but...my cuts will be bigger than yours'

Pre-contract Considerations

- Due diligence – who are you contacting with?
- The contract
 - In writing
 - complete, accurate, drafted to recognise the needs/requirements of the parties and of the Project itself
 - understand, and fully, the rights, entitlements and obligations

Relevant Contract Provisions

- Payment
- Set-off
- Step-in
- Off site materials
- How is “an insolvency event” addressed?
 - Termination
 - Default and damages

Other means of protection

- Warranties
 - What is it?
 - Step in for funders/employers
 - Payment for intellectual property
 - Set off wording
 - Is it needed?
- Bonds
 - default
 - on demand
 - Value – ordinarily 10%
 - Expiry
 - How is loss ascertained?
 - Insolvency wording

Other means of protection

- Parent Company Guarantee
 - Relevant
 - Is it needed?
- Off site materials
 - Vesting certificate
 - Materials bond
 - How useful? Respond quickly!
- Retentions
 - Likely to be 5, (2½) or (1½)%
 - Extremes of 15% and 2% possible!

The Overall Contractual Matrix

- Ensure 'back-back' arrangements throughout the Project
- Release of drawings/design information necessary for the Project

Project bank accounts

Funds paid into a designated account and released when certified and due; monies are held in the account on “Trust”

The tell-tale/early warning signs of insolvency

- On site/day-to-day:
 - De-manning of sites/sub contractors
 - Slow-down in performance of the Works
 - Plant, equipment and materials
 - Attempts to renegotiate:
 - ❖ Payment terms
 - ❖ Price
 - Increased number of disputes
 - ❖ Unjustified claims or extra charges to increase the amount payable
 - ❖ Non payment

The tell-tale/early warning signs of insolvency

- Off site
 - Ongoing financial monitoring
 - Court judgements
 - Sub-contractors/supply chain
 - Market intelligence
 - Parent/Associated Companies

The tell-tale/early warning signs of insolvency

- What to do:
 - Do not ignore
 - Review contract terms
 - ❖ payment
 - ❖ title and risk
 - ❖ set-off
 - ❖ assignment
 - ❖ termination

The tell-tale/early warning signs of insolvency

- Contingency plan
 - ensure you are not in breach eg. termination/repudiatory breach
- Monitor
 - First hand information on “insolvency event” essential
 - Progress of works
- Review site security
- Review terms of performance bonds/guarantees
- Open dialogue

An “Insolvency Event”

JCT Standard Building Contract 2005

- A party is insolvent if:
 - He enters into an arrangement, compromise or composition in satisfaction of his debts (clause 8.1.1); or
 - Without a declaration of insolvency, he passes a resolution or makes a determination that he be wound up (clause 8.1.2); or
 - He has a winding up order or bankruptcy order made against him (clause 8.1.3); or
 - He has appointed to him an administrator or administrative receiver (clause 8.1.4)

Different Types of Insolvency Events

- Administration
 - Designed to rescue the company or the business
 - Failing both of those, produce a better return for creditors than liquidation
 - Continued trading?
 - Moratorium
- Liquidation
 - Compulsory – court petition – company cannot pay debts
 - Voluntary - shareholders own decision
- Receivership
 - Superseded by Administration
 - Primary duty to bank appointing receiver
- Company Voluntary Arrangements
 - Agreement with creditors

How do you know?

- Winding up petitions
 - Central index of Royal Courts of Justice
- County court judgements
- Companies House
- Late/qualified accounts
- London Gazette