Issue No : 6
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Article No : 1
Author : Roger Trett
Title : Introductory Message

Unfortunately the economy seems to be bumping along the bottom for a much longer period than anticipated. It appears that none of the economists really know what is happening or the answer to it. It might be better if we ignored the gurus and decided to be optimistic and took positive steps to rejuvenate the industry at a time when development prices must be at their lowest for years. However I have my doubts that such unilateral positive moves will be made until someone, somewhere, actually tells us that things are getting better.

The recession in the construction industry is still hurting a large number of companies and is generating a lot of work for accountants and lawyers as well as ourselves. It does appear, however, that a considerable number of actions are being pursued for tactical reasons as opposed to the merits of the case. It is clear that a number of companies are holding on to money for as long as possible by raising spurious claims and/or counterclaims. The consequence is that a number of extremely capable Contractors and Sub-Contractors have gone and will go out of business due to lack of cash flow.

Perhaps this is one area where ADR could be of benefit in achieving settlements, although of course those companies that raise the spurious claims for tactical reasons would not subscribe to ADR as they rely upon the long legal process to achieve their ends. It is a pity that some interim method of assessing the merits of a case to alleviate cash flow problems where there is a genuine case is not available. The reaction might be that SC Order 29 provides just this remedy but bearing in mind that the time taken to get these from an initial claim presentation is quite substantial it does not really solve the problem. The high degree of certainty required to be successful at this stage also prohibits many awards.

Issue No : 6
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Article No : 2
Author : Mike K Marshall
Title : Designed to Confuse

In this, the first of a two part article Mike Marshall examines the intricacies of shared design responsibilities.

Introduction

I am concerned in this article with the complicated consequences of something going seriously wrong when the task of preparing the design for a construction project; or elements of it, Is shared between the parties, either expressly or by implication. .

Design is one of those words which seems to be used by most people in the belief that it has a clear and accepted meaning. However, as I am sure some readers will have realised, "design" means different. things to different people depending upon circumstances. This is perhaps not a major problem in the majority of commercial transactions where, to the ordinary man, the dividing line between the design and manufacturing processes of, say, a washing machine, is largely irrelevant. Since he is buying a complete product, he is interested only in whether or not it is suitable and is unconcerned about how the design is achieved.

Since construction projects are essentially unique events, the definition of design, and who is responsible for achieving it, is fundamental. The Employer must decide at the outset how the design is to be achieved and by whom. Ordinarily, he will adopt the traditional practice and have the project designed by an Architect or an Engineer; a Contractor will be selected once the design is at least well advanced, if not complete. Thus the design will be firmly in the hands of the Employer with construction, or the realisation of the design, in the hands of the Contractor. Design and construction might be considered almost as separate events, and the standard forms of contract generally used in building and civil engineering, emphasise this distinction.

I suppose the other end of the spectrum might be where an Employer decides to instruct a Contractor to design and build a six bedroom house, then embarks on a world cruise and returns when the house is complete!

This is the construction equivalent of buying our washing machine, but the occasions when a "one-off" project is defined in such a summary fashion must be rare.

In tile two examples I have mentioned, there is little doubt that the Employer is wholly responsible for design in the former case, whilst the Contractor is wholly responsible in the latter. The need for a precise definition of design, in each case, would really only come about if a dispute arose concerning some element of design or, more particularly, responsibility for it. So long as one party accepts total responsibility for the preparation of the design, enabling construction to be completed to the Employer's satisfaction, the necessity to precisely define the content of the design process is greatly diminished.

As we move away from these simple cases however, responsibility for design becomes increasingly difficult to be certain about. In recent years there has been a move towards involving the Contractor in design matters to a greater. extent as projects have become more complex; a shared or divided responsibility for design is thereby created. This development has occurred more so in the sectors of industrial plant and offshore oil structures than in building and civil engineering. Even so the trend seems to be widespread.

In some cases, the Contractor may be presented with a comprehensive and quite detailed design by the Employer at the tender stage, and is asked to adopt and develop this design. In others, the Employer may retain responsibility for key elements of design, but require the Contractor to carry out everything else. In yet another variation on this theme, the Contractor may be required. to develop a "design concept" presented to him by the Employer.

Given that we all have a slightly different idea of the precise meaning of design, in any particular context, it might readily be appreciated that failure to adequately define respective responsibilities for design in these "hybrid" arrangements, can lead to very complex disputes.

Whilst there are no simple answers to these difficulties, I have tried to outline some of the factors which readers, on both sides of the contractual fence, might bear in mind when contemplating any involvement with these "split design" type contracts.

Definition

Having begun by proposing that everyone has a different perception of the meaning of design, I had better try and provide a definition so we all know what we are talking about. First, some authorities.

The Oxford English Dictionary defines design as a mental plan; a purpose; the plan of a building; an arrangement of lines. This is perhaps too general for our purpose, although "a mental plan" is attractive when exploring the difficulties which arise, because, in many cases, the mental plan or concept is insufficiently translated.

In his book *Construction Contracts: Principles arid Policies in Tort and Contract* (Sweet & Maxwell 1986), Mr Duncan Wallace has included two excellent chapters on contractor's design. He has attempted a definition of design, and, whilst he says he does not claim special authority, I hope he won't mind if I refer to it now:

"'Design" includes the choice of quality or description of work materials and components as well as the dimensional or structural design of the final permanent work or product - so that the legal responsibilities arising from it may involve a wide range of concepts of structural soundness, durability, safety, working life, quality, suitability, amenity, ease of maintenance and satisfactory performance after completion".

I think many of us will probably find this definition a little difficult to remember and whilst we might regard it as legally reliable a more practical approach is needed.

Another definition is given in the *Building Contract Dictionary* (Vincent Powell-Smith and David Chappell, The Architectural Press 1985):

"'A rather vague term denoting a scheme or plan of action. In the construction industry it may be applied to the work of the architect in formulating the function, structure and appearance of a building or to a structural engineer in determining the sizes of structural members".

Well, at least this confirms what we already suspect; it's rather vague! Whilst I like the description of the architects work, I favour the following definition provided by Mr D L Comes, in his paper to the Construction Contract Policy Conference in 1988:

"All the decisions that have to be made as to the location in three dimensions of each and every component part of the project and the definition of the quality and quantity (including the specification of workmanship) of each component and how each component fits one with another".

Whilst at first glance these definitions seem to contain few things in common, they are, in fact, complementary. Thus the decisions referred to in the Cornes definition are those required to

complete the formulation stated in Powell-Smith's definition. Similarly, these decisions lead to the legal responsibilities listed in the Duncan Wallace version. Rather than attempt to devise a composite definition of my own, I think it best if we rely upon the Comes definition but remember the legal responsibilities arising from the formulation process.

Obligation of Designer

In any construction contract, whether it be traditional (i.e. designed by the Employer) or design and build, certain terms are usually to be implied (if not expressly stated). So far as design is concerned, these are:

1. to carry out the work in a workmanlike manner;
2. to use materials of good quality; and
3. that materials and work will he such as to render the completed works reasonably fit for purpose.

It is most unlikely that a Contractor would ever be relieved from complying with the first two, whatever the contractual arrangements are, with regard to design. However, in traditional contracts, where the Contractor's skill and care has not been relied upon by the Employer in the selection of components or materials, the fitness for purpose warranty will normally be excluded. Whilst the Contractor will probably be responsible for the quality of materials obtained in complying with the instructions inherent in the Employer's design, the actual selection of a particular type or, in some cases, the manufacturer of components or materials, and their configuration within the works, will be the Employer's responsibility.

In design and build contracts, the position is quite different. The Employer will normally rely upon the Contractor in selecting components, equipment and materials and, therefore, the fitness for purpose warranty almost certainly extends to design in this type of contract. Of course, this assumes that the Contractor has total responsibility for design and this has not been compromised by selective instructions given by the Employer. It is also necessary for the Employer to make known to the Contractor the purpose to which the finished works are to be put.

This principle was outlined in remarks made by Lord Denning in Greaves (Contractors) Ltd-v-Baynham Meikle & Partners in 1975:

"Now, as between the building owners and the contractors, it is plain that the owners' made known to the contractors the purpose for which the building was required so as to show that they relied on the contractor's skill and judgement. It was, therefore, the duty of the contractors to see that the finished work was reasonably fit for the purpose for which they knew it was required. It was not merely an obligation to use reasonable care, the contractors were obliged to ensure that the finished work was reasonably fit for the purpose".

Just to make matters even more complicated however, readers should note that in the only widely used standard form of contract devoted to design and build by the Contractor (JCT Standard Form of Building Contract with Contractor's Design) this principle is denied. In clause 2.5.1 we see that:

... the Contractor shall have in respect of any defect or insufficiency in ... design the like liability to the Employer ...as would an architect or... other appropriate professional designer holding himself out as competent to take on work for such design who, acting independently under a separate contract with the Employer, had supplied such design for ... works to be carried out ... by a building contractor not being the supplier of the design".

In those design and build contracts which do not incorporate the JCT standard terms we may assume that not only is there a mutual expectation by the parties that the design will be successful, but there is an implied term to the effect that the Contractor warrants that it will be.

This contrasts quite dramatically with the position of the designer in traditional contracts. Here, the Architect or Engineer, as the case may be, is commissioned to prepare the design to accord with the Employer's instructions. In the contract so formed, the designer undertakes to employ the appropriate level of skill and care in seeking to achieve the desired result, but does not guarantee the suitability or effectiveness of the design. I understand that the level of skill and care which is deemed to be appropriate is that which would be used by an ordinary professional man in normally undertaking his duties.

"Where you get a situation which involves the use of some special skill or competence, then the test as to whether there has been negligence or not is ... the standard of the ordinary skilled man exercising and professing to have that special skill".

(McNair J. in Bolam-v-Friern Hospital Management Committee (1957) 1 W.L.R.)

At first glance this may seem iniquitous from the Employer's point of view but the position is analogous to that of, say, a surgeon, whose duty it is to conduct an operation using appropriate skill and care. The operation may not be successful for any number of reasons, which the surgeon may not have been able to foresee or control. In civil engineering in particular, the number of uncertainties are legion, and the successful outcome of the project is obviously subject to these. Of course, the Employer can sue the designer if the design is faulty, not on the basis that it is unfit for purpose, but if the fault was the result of a failure on the designer's part to use reasonable skill and care; that he was professionally negligent.

I have explored this area of the obligations which a designer assumes at some length, since this embodies the vital difference between traditional and design and build contracts, so far as design is concerned. An awareness of this difference is even more important when considering contracts where design responsibility is divided or shared.

Part II will examine the practical implications of shared design

Issue No : 6
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Author : Roger Trett
Title : Overheads

Roger Trett looks at the difficulties associated with accurately ascertaining Head Office overheads.

Introduction

One of the most contentious areas in claims for delay and/or disruption is where the claimant is seeking to recover the overheads of the company where revenue has not been earned through productivity to defray the overhead costs.

The task of evaluating site overheads (preliminaries) when considering the effects of an extended site duration, provided of course that the extended period is for reasons that entitle the Contractor/Subcontractor to be awarded costs, is not a major problem and provided proper records are kept the resolution of such claims should be reached amicably.

The Off-Site or Head Office overheads create a much bigger problem in resolution. These costs are the Off-Site or Head Office Management costs of running the Site and will be affected by delays in Contract completion in similar fashion to Site Overheads. They may also be affected by disruption. Irrespective of the difficulty in quantifying them they are nevertheless recognised as a valid case for reimbursement as direct loss and/or expense.

The structure of most Contractors is in the form of a Head Office organisation servicing more than one contract, thus the various departments e.g. Estimating, Contract Management, Surveying etc. have to be paid for by a contribution from a number of contracts. Most Head Office staff are involved in a contract to varying degrees and it is difficult, if not impossible to properly allocate Head Office staff to each contract.

A Buyer, Accountant or Secretary, for instance, would be unlikely to make any meaningful apportionment of time, even if the will to do so was there.

In the case of Tate & Lyle-v-GLC (1982) it was held that an allocation of management time was necessary to establish the extent of the loss incurred. This was not done and an acknowledged head of loss was disallowed.

In the absence of this allocation the most common method of evaluation of head office overheads is the formula method which can, in my view, give a disproportionate weighting, particularly where a contract has been substantially extended but with little activity.

Hudsons Formula

There are two formulae in common use, the first being that known as the "Hudson" formula (page 599 of Hudsons Building Contracts 10th Edition). Additional Head Office overheads are equated as,

$$\frac{\text{H/O Profit Percentage}}{100} \times \frac{\text{Contract Sum}}{\text{Contract Period in weeks}} \times \text{Period of Delay (weeks)}$$

The Hudson formula has been used on many occasions and has also been endorsed by the Court in the case of Finnegan Ltd-v-Sheffield City Council (1988).

However, proper appraisal of the formula reveals that it is flawed, in that the application reimburses the Contractor not only overhead costs, but profit also. It is possible therefore that the Contractor could end up with a much greater profit than that included in his contract to start with. In addition the straight use of the formula may well provide the Contractor with an over-recovery of overheads in respect of his actual loss.

It must be remembered that the object of reimbursing loss and expense is equivalent to damages i.e. to put the Contractor in the position he would have been but for the breach.

The direct loss and/or expenses arises from the first rule of Hadley-v- Baxendale in that the Contractor is back where he started i.e. earning his original profit.

Profit however, can be recovered as "special" damage under the second rule of Hadley-v.Baxendale in the loss of the profit earning capacity which the Contractor is denied earning through prolongation of the contract. This is based upon the fact that the Contractor has limited resources of staff, plant, capital etc., and if these are tied up they can only by virtue of the first rule produce the profit which is in the contract in the first place and they are denied the opportunity, because of their commitment, from earning money elsewhere, which the Contractor must do to exist. However, it is necessary to demonstrate that work was available that would have been secured prior to recovery of profit.

A further flaw in the straightforward use of formula is that it deals with the original contract value and does not take into account any additional recovery of overheads and profit through variation adjustments nor does it take into account the general trading of the Company as a whole.

In the above context we can see that the straight use of the Hudson formula appears to conflict with the basic common law principle of recovery of loss and expense.

It must be pointed out, however, that Hudson does qualify the use of the formula when looking at the profit element and assumes that "the profit budgeted for by the Contractor in his prices was in fact capable of being earned by him elsewhere had the Contractor been free to leave the delayed contract at the proper time".

This qualification is conveniently ignored by many claim presentations. The formula still suffers from the criticisms however.

Emdens Formula

The second commonly used formula is Emden's formula published in Emden's Building Contracts and Practice 8th Edition, Volume 2,

Total Company Overhead & Profit

$$\frac{\text{Turnover Percentage}}{100} \times \frac{\text{Contract Sum}}{\text{Contract Period in weeks}} \times \text{Period of Delay (weeks)}$$

This formula is more realistic in that it relates to the overhead and profit situation of the company as a whole, rather than the individual contract. Nevertheless, it can be criticised for blind usage as much as the improper use of the Hudson formula.

Whilst the principle of loss of contribution to head office overheads is well accepted there may be a number of cases where no contract loss is incurred.

A well run business will budget on the basis of a certain number of contracts, and structures its staff to suit the workload. A company surveyor or contracts manager may, for example, be able to handle four contracts. In theory if one overruns they are unable to cope with a new

one until the existing one is complete. The costs of the Surveyor/Contracts Manager etc. still have to be met but the loss of contribution, assuming four equal size contracts, would be 25% for the period overrun. In reality, however, most contractors are flexible and would not let a contract go due to lack of head office staff. What may well happen is the relevant staff would tend to work harder and input longer hours, thus the contribution from the next project would make up the deficiency and no loss would occur.

What is the position if the Contractor recovers his Head Office overheads on his year's trading irrespective of a contract that has overrun? He may have ended up with a reduced profit for the year but does the claim become a loss of profit claim or can it be distinguished as a loss of overhead claim in relation to the particular project that overran?

What happens if the Contractor makes an over-recovery of Overheads from some contracts? Can they be used to set-off the losses made on a particular contract if the company overheads have been fully recovered?

From the above it will be seen that the matter is not clear cut and that the use of formulae cannot be utilised without consideration of many other aspects. The only real way to seek recovery of loss is to keep definitive records.

Disruption and Acceleration

In the instance of disruption and/or acceleration there may well be the need to provide additional overhead resources to re-organise etc. Thus a contribution to cover the costs of those resources will be required as the measure of expense arising therefrom. The only proper way to evaluate this contribution is to keep records of the application of those resources.

Another area of potential overstatement of a claim for loss of overheads is where a "global" claim is submitted. This claim seeks to determine that the loss of overhead recovery is evaluated by taking the number of hours expended multiplied by the contractors costing rate, which includes a percentage for Head Office Overheads. The Contractor then seeks to show that he should have recovered an overhead value based upon hours expended less hours planned on the project.

This approach is unacceptable not only because of its global nature, but also tends to overstate the overhead contribution that the contractor should have returned. The application of an Overhead rate per hour takes no account of the actual level of Overheads needed to be recovered by the Contractor. For example, if he planned to work 40 hours per week at tender stage, and for reasons which provide an entitlement to recover his additional costs, works 60 hours per week, the application of the overhead per hour to his costs will grossly inflate the overhead recovery of the company and similarly inflate any claim.

Conclusion

There is no clear cut avenue upon which to evaluate overhead losses and as with any matter of contention no strict manner of evaluation will be applicable. Each matter will necessitate examination and have to be treated on its merits at the time.

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Author : Ken Salmon
Title : Set On Set-Off

When one party to a contract (A) is on the receiving end of a claim from the other party (B), and A himself has a claim against B, A will wish so far as possible to use his own claim to extinguish or reduce B's claim. If he is able to do so he will be exercising the right of set-off. The standard forms of Main Contract common in use in the Construction Industry do not contain specific rights of set-off. Instead they often contain rights to withhold or deduct monetary claims, from monies otherwise due.

Rights of set-off are, however, common in the standard forms of Sub-contract in the Construction Industry, and in the various hybrid sets of conditions, which Main Contractors will seek to impose on Sub-contractors and suppliers.

What is a set-off?

At Common law and in Equity the right to make a monetary cross claim to reduce or extinguish an incoming claim is called a right of set-off. A true set-off is a Defence and as such may be used as a shield not as a sword. Despite this general rule, if the amount of the cross-claim is closely connected with the subject matter of the original claim, then it may be used offensively, as a sword, and then it is called a counterclaim. A set-off must be the subject of a counterclaim where it exceeds the amount of the original claim, or where it may be desired to continue with the cross-claim even though the original claim is not proceeded with.

A true counterclaim is not a Defence but a distinct and separate cross-claim. It may or may not be connected with the subject matter of the original claim. It may even arise after proceedings have been commenced on the original claim. Any cross-claim may be the subject of a counterclaim (subject to limited exceptions unlikely to be encountered in construction disputes).

Both a setoff and a counterclaim may be for a fixed sum or for damages which have not yet been quantified. Examples of allowable set-off in construction disputes are:

1. The employer claims liquidated and ascertained damages by way of set-off, or by way of counterclaim where they exceed the original claim, in response to a claim for payment by a contractor for work done.

1. A purchaser of goods claims damages for breach of warranty of fitness for purpose in response to a claim for the price of the goods supplied.

1. A building owner sets-off a cross-claim for defects in answer to an action for the price of work done by a builder.

Contractual right of set-off

The parties may by their contract modify (either by restricting or enlarging) the types of cross-claim which can be made, or the circumstances in which such cross-claims can be made.

Example: the Parties to a contract agree that either may set-off any cross-claim arising under any other contract between them.

All the standard forms of sub-contract published by the Joint Contracts Tribunal (JCT) contain an express right of set-off in favour of the Main Contractor against the Sub-contractor. The clauses in these contracts. have these features in common.

1. The specific right of set off is given to the exclusion of all (or some) of the Common Law or Equitable rights of set-off.
2. The right is expressed as one to set-off "loss and/or expense" which has "actually been incurred".
3. The clauses are almost always subject to a notice of intention to set-off being first given, the set-off being quantified in detail and with reasonable accuracy, and the Notice being given within certain time limits.
4. Some contracts have the additional requirement that the Architect or Supervising Officer has issued a Certificate of Non-Completion.

The JCT Contracts in common use are:

- The BEC 1971 Edition revised July 1978 for non-nominated Subcontractors (the Blue Form). The set-off provision is contained in Clause 15.
- The NFBTE/FASS/CASEC Domestic Sub-Contract DOM/I 1980 (known as DOM/I). The setoff provision will be found in Clause 23.
- The JCT Nominated Sub-Contract NSC 4. The set-off provision is in Clause 23.
- The IFC Sub-Contract NAM/SC 1984 (NAM 4) for use when the Sub-Contractor is named by the Architect. The set-off provision is in Clause 21.

Conditions

Unless the amount proposed to be set-off is agreed or has been the subject of an Award by an Arbitrator, the following conditions must be satisfied:

1. The loss and/or expense must have actually been incurred. It must not be future loss nor a mere liability nor a contingent loss.
2. The loss or expense must have been incurred by reason of a breach of or failure to observe the provisions of the Sub-Contract by the Sub-Contractor'. This will exclude fights arising outside the contract. Contrast hybrid forms where the right of set-off is not always limited to rights under the contract.
3. The set-off must have been quantified in detail and with reasonable accuracy by the Contractor. The detailed and accurate quantification must be in or accompany the notice.
4. The contractor must give notice of his intention to set-off the amount quantified and the grounds on which the set-off is to be made. It is good practice but not essential to refer to the set-off clause by number.
   NB: The Notice must be given (not just sent or posted) not less than a specific period before the money from which the set-off is to be made, becomes due and payable to the Sub-Contractor.
5. In the case of NSC/4 there is a further condition which is that no set-off for delay may be made unless the Architect or Supervising Officer has issued a Certificate of Non-Completion under Clause 35.15 of the Main Contract in accordance with Clause 12.2 of the Sub-Contract and copied the same in duplicate to the Sub-Contractor.
   Note: this does not apply to set-off for reasons other than delay e.g. defective work or damage to the main contract works.

1. These Clauses also have in common an exclusion of any other right of set~ff. Thus if the Contractor fails to exercise his right under and in accordance with the Contract, he cannot rely on ~ common law or equitable right of set-off to defect a Sub~ontractor's claim for payment based on an Interim Payment Certificate, application or valuation.

Cases

In *Chatbrown-v-McAlpine (1986 Court of Appeal)* a case on The Blue Form, it was held at first instance and confirmed by the Court of Appeal that the loss and expense must have actually been incurred i.e. lost or paid out before the date the notice was given. The Court in passing gave the opinion that claims for disruption might be easier to justify than claims for delay. Thus, when work is defective, the cost of remedials will have been "incurred" when an account has been received (and preferably paid). In the case of disruption the cost of labour and plant standing idle, or the cost of extra resources, will have been "incurred" when expended, assuming that such costs are not otherwise recoverable. In the case of delay, however, it may be difficult to show that the cost of downtime, or extra resources to make up lost time, were actually incurred at the time the delay was operating since it will not be apparent until completion whether the main contract works have been delayed. These may be regarded as being costs which would have been incurred in keeping the site open in any event. This is less of a problem once the Contract overruns and there is a prolongation claim.

In *Archital Luxfer Limited and A. J. Dunning & Son (1987 Court of Appeal)* it was held confirming McAlpine and Chatbrown, that the loss and expense must have been incurred at the date the notice was given. This was a case on NSC/4 and the Court held "arguably" all the conditions for set-off had been satisfied, which defeated the Sub-Contractor's claim to summary judgement for payments due upon Certificates. This was a sympathetic decision and it is unsafe to rely on "arguable" compliance.

In *BWP (Architectural) Limited and Beaver Building Systems (1988)* a decision of the Senior Official Referee, it was held that a Main Contractor had to operate the set-off provisions, even where he merely wished to challenge the Sub-Contractor's valuation on the ground that the work was worth less than the value claimed, or that the work had not been properly executed. This decision was subsequently disapproved by the Court of Appeal in the case of *ACSIM-v-Danish Contracting & Developing Co. Limited (1988, 4BLR p55)*. The Court of Appeal held that if the Main Contractor merely wished to challenge on credible evidence, the amount of the Sub-contractor's valuation or payment application, on the grounds that it included the value of work not done or not done properly, or that the work was worth less than that claimed by reason of some breach of the Sub-Contrct conditions, or it was erroneously calculated, then the Main Contractor could do so without having to apply the set-off provisions. These were true Defences and the set-off provisions did not apply. The Main Contractor may therefore pay less than applied for, but it would seem advisable to give good reasons for so doing. For example the sum applied for exceeds the total value of the Subcontract works properly executed or that the works are incomplete and therefore worth less than the valuation claimed, or that there is an arithmetical error in the application.

This was followed in *Mellowes PPG Limited-v-Snelling Construction Limited (1990) 49BLR 109* the Deputy Judge holding that the right of the Main Contractor to deduct from monies due to the Sub-contractor under Clause 21.3.1.2 of NSC/4 was separate and distinct from the right to set off under Clause 23. The set-off procedure under Clause 23 did not have to be followed for a deduction under Clause 21. Furthermore since the main contract did not entitle the employer to make a deduction from the Main Contractor on account of delay by a nominated Sub-contractor, such deduction as was in fact made, could not be the proper subject of a deduction under Clause 21, by the Contractor against the Subcontractor.

In *Scobie and McIntosh Limited-v-Clayton Bowmore Limited (1990) 49 BLR 119*, the Plaintiff Sub-contractor obtained a judgement for the value of the work done less a specific sum for defects, arguments as to which were stayed to arbitration. It was held that the Sub-contractor's right to payment from the Contract was not, on a true construction of Clause 23 of NSC/4A dependent upon certification by the employer under the Main Contract. The contracts were entire, separate and distinct. Neither did the Sub-contractor's right to compensation for unlawful termination, depend on the provision of NSC/4A. When the contract was repudiated, the law imposed an obligation upon the party in default to compensate the innocent party.

Conclusions

Set-off is an area which has given rise to a considerable number of cases and numerous disputes. It is only an effective weapon if used properly. Whether Contractor or Subcontractor be astute to check that all and every condition upon which the right depends has been properly exercised. Read the Conditions of the Contract. Study the terrns of the Notice. If you are in doubt do not hesitate to take professional advice. Three common mistakes are:

(a) Failing to give at the Notice in due times.

Example: Clause 23.2 of DOM/l provides that the Notice "shall be given not less than 20 days before the money from which the amount or part thereof is to be set-off becomes due and payable to the Sub-contractor;" for "given" read "Received". Merely because the Notice is posted in good time does not mean it will arrive in good time. If necessary the Notice should be sent by fax and/or by Recorded Delivery or Registered Post, or by Courier, or by hand. Exclude the day the Notice is given, and the day it is received from the calculation of the 20 days. This avoids arguments on calculating the period. In an unreported decision, it has been held by an Official Referee in London, that in respect of DOM/1 the. first payment becomes due one month after the date of commencement of works on site, and is then payable 14 days after. Interim payments thereafter become due monthly payable 14 days after the due date. Therefore any notice in respect of the first payment would have to be given at least 6 clear days before the end of one month after commencement of works on site.

(b) Failure to state the grounds on which the set-off is to be made.

Example: It will not be sufficient to recite in the Notice that a setoff is to be made by reason of a breach of or failure to observe the provisions of the Subcontract. The breach or failure to observe the provisions of the Subcontract must be identified. Thus if loss and/or expense has been incurred by reason of the Sub-Contractor's failure to proceed regularly and diligently with the works, or by reason of his failure to execute the works properly in accordance with the Sub-contract this should be stated and brief particulars given. It is unsafe to refer to other documents which do not accompany the Notice. If reference is to be made to other documents, for particulars of the breach or failure to observe the terms of the Subcontract, then they should not only be referred to in the Notice, but copies should accompany the Notice.

(c) A failure to quantify the loss and/or expense in detail and with reasonable accuracy.

Example: It is insufficient to say "cost of delay per week £1,000 x 4 equals £4,000". The constituents of the sum of £1,000 should be set out identifying the weekly costs of labour, plant and equipment, establishment costs (not otherwise recovered under the terms of the Main Contract). Similarly with disruption costs, constituent elements should be identified and reasonably accurately quantified.

One final note of caution. Special care is needed where the conditions as to payment and/or set-off have been amended, or additional or supplementary terms have been agreed; these must be analysed to see what effect (if any) they have upon the set-off provisions.

This is believed to be a correct Statement of the Law as at March 1992.