

Holmwood Holdings Pty Ltd v Halkat Electrical Contractors Pty Ltd [2005] NSWSC 1129

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This decision of Brereton J has important ramifications for adjudicators. Firstly, in order to properly found jurisdiction, an adjudicator need consider only those provisions of the contract which are relevant to the adjudication application. Secondly, an incorrect interpretation of a contractual provision by an adjudicator does not necessarily invalidate a determination; a failure to consider the relevant provision would. Recklessness or capriciousness on the part of an adjudicator, such as to establish the absence of a genuine or conscientious attempt to perform the adjudicator's function, short of a willful and deliberate failure to attempt to perform the function, can amount to a want of good faith.

Background

On 16 September 2004 Holmwood Holdings Pty Ltd ('Holmwood') entered into a construction contract with Halkat Electrical Contractors Pty Ltd ('Halkat') for the provision of certain electrical works in relation to the refurbishment of a nursing home at Bexley, New South Wales.

On 3 June 2005, Halkat made a payment claim under the *Building and Construction Industry Security of Payment Act NSW 1999* (the 'Act') for \$127,406.67. The claim identified, for each element of the works, the contract sum attributable to that element, the percentage claimed to date and the amount claimed. However in several instances, the amount claimed did not reflect the claimed percentage of the contract sum. The claim also stated that certain drawings were attached which provided an indication of how the percentages were derived, but no drawings were provided with the claim.

Holmwood provided a payment schedule within time, which provided different values for the works and detailed some deductions which Holmwood had made (for example by way of liquidated damages and the retention) with the result that Halkat owed Holmwood the sum of \$83,265.50.

Halkat made an adjudication application on 27 June 2005, which did include the drawings missing from the payment claim. Holmwood's adjudication response, issued on 5 July 2005, raised two jurisdictional grounds as follows:

1. there was no construction contract between the parties as the principal was named in the contract as 'Homewood' not 'Holmwood';
2. the payment claim was not validly served as it was served by Halkat's solicitor, not Halkat personally.

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Five non-jurisdictional grounds for withholding payment were raised the first, and the most important of which, was that Holmwood claimed that Halkat had already received excess payment for the work it had done. Holmwood valued the completed work at \$59,376 (before deductions in the sum of \$90,707) whereas Halkat claimed the value of work completed was \$152,000.

The Determination

The adjudicator gave his determination on 7 July 2005. He determined the progress payment to be payable to Halkat was \$116,593.35. He rejected Holmwood's argument regarding service of the payment claim and also rejected Holmwood's argument regarding the identity of the principal. The adjudicator considered this argument was 'totally lacking in merit' and considered that this influenced the creditworthiness of Holmwood's other submissions.

The last four non-jurisdictional grounds were also rejected by the adjudicator, and had no bearing on the appeal. However in relation to the first non-jurisdictional ground, the adjudicator was faced with two different valuations of the work carried out. The adjudicator did not consider the deduction of liquidated damages to be valid, and, considering the unmeritorious arguments put forward by Holmwood, preferred Halkat's valuation of the works.

The Appeal

Holmwood sought a declaration that the determination was void and of no effect on the following 3 grounds:

1. the adjudicator failed to comply with the basic and essential requirements of the Act as he failed to consider the provisions of the construction contract;
2. the determination was not an attempt in good faith, by the adjudicator, to exercise the powers available to him under the Act; and
3. Holmwood had been denied natural justice because:
 - (i) Halkat's payment claim was incomplete;
 - (ii) drawings were included in the adjudication application which were stated to be included in the payment claim but which, in fact, were not; and
 - (iii) the adjudicator determined the value of works based on matters related to credit in relation to which no submission had been made.

The matter came before Brereton J on 16 September 2005 who addressed each of the three points raised above.

1. Failure to consider relevant parts of the contract

Holmwood made three submissions on this point. Firstly, Holmwood argued that as the adjudicator was not provided with the specification and certain plans, he could not possibly have considered the entirety of the contract. Secondly, the adjudicator determined the due date for payment to be 21 June 2005, when a proper consideration of the contract would have led the adjudicator to determine an entirely different date. Finally, Holmwood argued that the adjudicator failed to allow for the retention in his determination.

Section 22(2)(b) of the Act requires the adjudicator to consider the construction contract in question. Brereton J considered whether this section required the adjudicator to consider all of the sections of the construction contract. Under his interpretation of the case of *Brodyn Pty Ltd v Davenport* (2004) 61 NSWLR 421, for a determination to be valid, the adjudicator had to consider the matters specified in s 22(2), although error in considering those matters, so long as they were in fact considered, would not invalidate the determination.

This, however, did not mean that the adjudicator was required to consider every provision of the construction contract, merely those ones that were relevant to the adjudication application. A failure by the adjudicator to consider relevant provisions of the construction contract would amount to jurisdictional error resulting in invalidity of the determination. However, as the plans and specifications not considered by the adjudicator would not have impacted on his determination and were not relevant to the adjudication, Holmwood's argument failed.

In relation to the due date for payment, the adjudicator concluded that as neither party had made a submission as to the due date, the due date would be 21 June 2005, being 10 business days after the date of service of the payment claim. The adjudicator did not refer to part D of the schedule to the contract which provided for the contractor to be paid within 30 days of the date of the claim.

Brereton J concluded that if the adjudicator had wrongly interpreted the contractual provisions and arrived at the wrong date for payment, this would not invalidate the determination. However where the adjudicator did not refer to the relevant contractual provisions at all, it could be inferred that the adjudicator did not in fact consider a relevant provision of the contract. This failure would invalidate the determination.

Holmwood's third argument was that when determining the amount payable, the adjudicator did not consider the deduction of the retention pursuant to clause 13(a) of the contract which provided for 10% of the moneys payable under the contract to be retained by the principal until 5% of the contract sum had been retained. There was nothing in the determination demonstrating that the adjudicator considered clause 13(a) and it could be inferred from this, that the adjudicator did not consider this part of the contract. Again, a complete failure to have regard to this relevant provision of the construction contract would be sufficient to invalidate the determination.

Brereton J concluded that if the adjudicator's errors were of no practical significance, for example, if they related solely to the due date for payment, there might be an argument that Holmwood should not be entitled to any relief. However in this case, the failure to have regard to the retention affected the quantum of the adjudicator's decision and therefore the invalidity extended to the determination as a whole.

Failure by the Adjudicator to Act in Good Faith

Holmwood argued that the decision-making process of the adjudicator did not amount to a good faith attempt to determine the dispute. Holmwood's payment schedule raised issues concerning the percentage of works stated to have been completed and the resulting amounts payable to Halkat.

The adjudicator did not address these issues, but decided that he preferred Halkat's valuation of the works performed as Holmwood had raised some unmeritorious arguments in its adjudication response. The adjudicator stated:

In deciding whether to adopt the assessment of the claimant or that of the respondent I am mindful of the respondent's unmeritorious challenges to the validity of the payment claim [the allegation that the respondent was not a party to the construction contract and that service by an agent is not valid service] and the respondent's completely unjustified deduction of alleged liquidated damages of \$89,100. In the light of these matters I am more inclined to believe the claimant rather than the respondent and I will adopt the claimant's valuation of \$152,000 in preference to the respondent's valuation of \$59,376 for the value of completed work before adding the amount for variations.

Holmwood argued that this did not amount to a bona fide attempt by the adjudicator to exercise the powers available to him. Brereton J reviewed the case law regarding the requirement of good faith, particularly in the immigration context. From these cases, Brereton J concluded that recklessness or capriciousness on the part of an adjudicator, such as to establish the absence of a genuine or conscientious attempt to perform the adjudicator's function, short of a willful and deliberate failure to attempt to perform the function, can amount to a want of good faith.

Turning to the adjudication, Brereton J did not consider that the adjudicator had met the requirements of acting in good faith. While the adjudicator was faced with bare assertion against bare assertion, he should have endeavoured to evaluate the payment claim in the light of the payment schedule using the evidence submitted as part of the adjudication application and the adjudication response, or, if necessary, using the additional powers available to him, such as calling a conference between the parties, or requesting further submissions. Brereton J said:

The quality of his determination in that respect did not differ from one based on a mere like or dislike of a party, based on unrelated conduct of the party. His ultimate determination, which depended upon acceptance in that way of Halkat's claim, was therefore not the product of a good faith attempt at performing his function, but of caprice.

The determination was therefore void as the adjudicator had not made his determination in good faith.

Denial of Natural Justice

The final ground on which Holmwood challenged the determination was that there had been a denial of natural justice, or a lack of procedural fairness during the adjudication process. Two arguments were raised in relation to this ground:

1. Holmwood was denied natural justice as documents were included in the adjudication application which were not previously included in the payment claim. The payment claim was therefore incomplete and invalid;
2. the adjudicator determined the value of the works performed by Halkat on the basis of findings of credit on which Holmwood had no opportunity to make any submissions.

In relation to the first point, Brereton J did not consider that there had been a denial of natural justice. Brereton J referred to the case of *John Holland Pty Ltd v Cardno MBK (NSW) Pty Ltd* [2004] NSWSC 258. While a respondent is not able, in its adjudication response, to raise reasons for withholding payment which have not already been included in its payment schedule, and an adjudication application may not include matters which go beyond the matters raised in the payment claim, this does not mean that materials not included in the payment claim can not be included in an adjudication response. The test is whether the additional material is or is not included within the scope or the ambit of the payment claim.

In this particular case, Brereton J concluded that the absence of the drawings did not prevent Holmwood disputing the amount of work performed by Halkat. The drawings were referred to in the payment claim and Holmwood was on notice of the arguments to be advanced by Halkat in its adjudication application. Holmwood was not deprived of the ability to raise arguments in response and while the drawings provided evidence of the works Halkat stated to have performed, the drawings were entirely within the scope of the payment claim. In addition, Holmwood was provided with the drawings in the adjudication application and was therefore able to respond to them in its adjudication response. There was therefore no denial of natural justice in this regard.

In relation to Holmwood's second point, Brereton J again, did not consider that there has been a denial of natural justice. Brereton J referred to the *John Holland* case and noted that if an adjudicator proposed to make a determination on a basis put forward by neither party to the adjudication, then natural justice required the adjudicator to inform the parties of the basis being considered by the adjudicator so the parties could provide their submissions on it.

However this duty did not extend to giving a party notice that the adjudicator preferred one party's valuation over that put forward by the other party. The adjudicator's decision to prefer Halkat's valuation over Holmwood's was sufficiently within the scope of the dispute as to negate any need for further notification to be given to Holmwood to allow it the opportunity to provide further submissions.

Conclusion and Comment

Brereton J supported the adjudicator's rejection of Holmwood's argument regarding service of the payment claim. Payment claims may therefore be served by agents of the claimant, including solicitors. It is now clear that a failure to consider relevant terms of a construction contract may potentially invalidate a determination. Such a failure may be inferred through the adjudicator not addressing the relevant provisions in his decision.

In adopting Halkat's valuation because Holmwood had put forward some unmeritorious arguments without considering the issues raised by Holmwood in its payment schedule, the adjudicator did not attempt, in good faith, to perform his function. The determination was therefore void as it was not the result of a genuine and conscientious attempt by the adjudicator to fulfill his role.

However this finding that the adjudicator did not act in good faith could potentially expose the adjudicator to liability as the indemnity provision in the Act (which is almost identical to the equivalent provision in the Queensland legislation) only protects the adjudicator from liability for things done, or omitted to be done 'in good faith in exercising the adjudicator's functions under the Act'.

Adjudicators should therefore ensure they act in good faith when making their determinations and consider all of the issues raised by the parties. A failure to do so could prove to be costly for an unwitting adjudicator.

