#137

IN THE HIGH COURT OF NEW ZEALAND
NAPIER REGISTRY

CIV-2011-441-54

	BETWEEN	HERBERT CONSTRUCTION COMPANY LIMITED Plaintiff
	AND	TUCK CONTRACTORS LIMITED (IN LIQUIDATION) Defendant

Hearing: 16 June 2011
(Heard at Napier)

Counsel: D.J. O'Connor - Counsel for Plaintiff
B. W. Gilmour - Counsel for Defendant

Judgment: 22 July 2011 at 11:30 AM

JUDGMENT OF ASSOCIATE JUDGE D.I. GENDALL

This judgment was delivered by Associate Judge Gendall on 22 July 2011 at 11.30 am under r 11.5 of the High Court Rules.

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Introduction

[1] Before me is an application by Herbert Construction Company Ltd (Herbert) to set aside a statutory demand issued by Tuck Contractors Ltd (in liquidation) (Tuck) for the sum of $24,577.03. That application is opposed.

[2] In summary, the grounds advanced in support of the setting aside application are that:

(a) there is a substantial dispute whether or not the debt is owed;

(b) Herbert has a counter-claim which exceeds the sum of $24,577.03 in the statutory demand; and

(c) Herbert is solvent.

Background

[3] Tuck was Herbert's sub-contractor in two separate matters:

i. The production and laying of concrete for part of a taxiway for aeroplanes at Hawke's Bay Airport (for which the sum of $22,290.80 is claimed to be outstanding);

ii. Work done on the Guardian Trust building in Hastings (for which the sum of $2,286.23 is claimed to be outstanding).

The statutory demand relates to the alleged non payment by Herbert of these amounts.

[4] With regard to the work at Hawke's Bay Airport, in 2009 Herbert as head contractor was contracted by Skyline Aviation Ltd (Skyline) to carry out work at the airport erecting an aircraft hangar, forming an apron outside the hangar and a taxiway and associated carparking, fencing and landscaping (the Head Contract). Herbert subcontracted work relating to the taxiway and apron to Tuck. In August 2009 Tuck says it completed its work. Over the construction period, five invoices had been delivered to Herbert. Four out of the five had been paid. The unpaid invoice was issued on 28 July 2009. It claimed $30,076.20 as the amount outstanding, and of that the $22,290.80 in question here remains unpaid.

[5] On 21 August 2009 a practical completion certificate for the Head Contract was issued by the engineer to that contract, Russell Grant Nettlingham (Mr Nettlingham), after a site visit on 7 August 2009 (Mr Nettlingham deposes to having so completed the certificate).

A list of defective work to be remedied was also compiled by Mr Nettlingham and he deposes to those defects having subsequently been remedied. A period of defects liability under the contract continued for three months from that date (7 August 2009 to 7 November 2009). While the practical completion certificate records that the original was sent to Herbert, Herbert denies ever having received the certificate. It is common ground, however, that no certificate of final completion under the Head Contract was issued.

[6] In so far as work on the Guardian Trust building is concerned, Herbert subcontracted Tuck to complete site works including the excavation and preparation for a concrete foundation and for wall panels. This included back filling and compaction for the foundation. Work was carried out and on 30 November 2009 an invoice for $24,752.25 was delivered to Herbert. Of this, $2,286.23 remains unpaid.

[7] On 23 December 2010, Tuck sent a letter of demand with respect to this sum to Herbert's office. After no response was received (Herbert says that is because its office was closed during the holiday period) a statutory demand was issued on 21 January 2011.

Counsels' Submissions and My Decision

[8] Herbert brings this application pursuant to s 290 Companies Act 1993. This sets out the basis on which a statutory demand may be set aside:

> **290 Court may set aside statutory demand**
>
> (1) The Court may, on the application of the company, set aside a statutory demand.
>
> ...
>
> (4) The Court may grant an application to set aside a statutory demand if it is satisfied that—
>
> (a) There is a substantial dispute whether or not the debt is owing or is due; or
>
> (b) The company appears to have a counterclaim, set-off, or cross-demand and the amount specified in the demand less the amount of the counterclaim, set-off, or cross-demand is less than the prescribed amount; or
>
> (c) The demand ought to be set aside on other grounds.

[9] Section 290(4)(a) requires an applicant to show a fairly arguable basis upon which it is not liable for the amount claimed in the statutory demand: *Queen City Residential Limited v Patterson Co Partners Architects (No 2)* [1995] 3 NZLR 307; *United Homes (1988) Limited v Workman* [2001] 3 NZLR 447 at 451-452. It must show that there is a genuine and

substantial dispute as to the existence of the debt: *Taxi Trucks Limited v Nicholson* [1989] 2 NZLR 297. Whether there is a "substantial dispute" is a question of fact to be determined in light of all the relevant circumstances: *Lockwood Buildings Ltd v Hunter Douglas Coilcoaters Ltd* (1988) 4 NZCLC 64,295. What an applicant does not have to show, however, is that it is impossible for the respondent to succeed in its claim against the applicant: *NZ Factors Ltd v Farmers Trading Co Ltd* [1992] 3 NZLR 703 at 708. Rather, the application must show a fairly arguable basis on which it is not liable for the amount claimed.

[10] Herbert's Application to Set-Aside the Statutory Demand lists as its grounds in support of the application first, that there is a substantial dispute whether or not the debt claimed is owing, secondly, that Herbert had a counterclaim equal to or exceeding the amount of Tuck's claim and thirdly, the use of the statutory demand procedure here amounted to an abuse of process.

[11] The issue for determination here, in my view, is a discreet one. The debts which are the subject of the present application are subject to the Construction Contracts Act 2002.

[12] Section 79 Construction Contracts Act 2002 provides:

> **79 Proceedings for recovery of debt not affected by counter-claim, set-off or cross-demand**
>
> In any proceedings for the recovery of a debt under s 23 or s 24 or s 59, the Court must not give effect to any counter-claim, set-off or cross-demand raised by any party to those proceedings other than a set-off of a liquidated amount if –
>
> (a) judgment has been entered for that amount; or
>
> (b) there is not in fact any dispute between the parties in relation to the claim for that amount.

[13] Although as Brookers Insolvency Law and Practice at para IN17.10(p) noted, there was originally some disagreement between the authorities regarding the effect of s 79 Construction Contracts Act 2002 leading up to the decision of the Court of Appeal in *Laywood & Rees v Holmes Construction Limited*, there can be no doubt now that this decision provides an unequivocal resolution of the principles which are to apply in situations such as the present one facing this Court.

[14] The grounds for allowing a counter-claim or set-off set out in s 79 Construction Contracts Act 2002 require the existence of a liquidated sum for which there is either a judgment or no dispute between the parties. In the present case the judgment debtor has not

obtained judgment for any amount by way of counter-claim or set-off nor can it be said that there is "no dispute" between the parties in relation to any claim it may have. On the evidence before me, any such claim is clearly disputed by the judgment creditor.

[15] In this regard, the Court of Appeal in *Laywood & Rees* stated:

> [61] We emphasise at this point the distinction between an application to set aside a bankruptcy notice or a statutory demand on the one hand and an adjudication of bankruptcy or order to wind up a company on the other. The question we are asked to resolve concerns the former. In that context, we prefer the view expressed by Randerson J in *Volcanic Investments*. We find some assistance in the exceptions provided for in s 79. Under that section, a set-off may be taken into account in debt recovery proceedings (including the s 73 process) if it relates to a liquidated amount and either judgment has been entered for that amount or there is no dispute between the parties in relation to the claim for that amount. Absent that, a determination can be entered as a judgment under s 73 and enforcement proceedings taken through the District Court, and any counterclaim, set-off or cross-claim must be pursued through separate proceedings.
>
> [62] If that is the position in relation to the enforcement processes available through the District Court, or where there is a charging order under the CCA, there seems in principle to be no reason why it should not apply in respect of a bankruptcy notice under s 19(1)(d) of the Insolvency Act or a statutory demand under the Companies Act. It is true that such processes have an additional dimension to them, in the sense that ultimately they lead to a process which focuses on liquidity and asset worth. It is also true, as Associate Judge Doogue said, that bankruptcy and liquidation proceedings have a broader objective than simply ensuring that a particular creditor is paid. Despite that, bankruptcy notices and statutory demands are, in a practical sense, important enforcement mechanisms, as Randerson J recognised. And in the present case, the debt which Holmes Construction seeks to recover has the force of a court judgment behind it. This is not a case where a creditor has sought to use bankruptcy or liquidation proceedings to recover a small amount from a person or company which can plainly afford to pay it.
>
> [63] If the contrary view were to be adopted, the efficacy of the s 73 process would, in our view, be undermined. Parties to construction contracts could refuse to pay an amount ordered by an adjudicator, and resist bankruptcy notices or statutory demands in relation to the debt, on the basis that they had a counterclaim, set-off or cross-demand. The effect of this would simply be to recreate similar problems to those which led to the enactment of the CCA, albeit in a different context.
>
> [64] We acknowledge that this approach may produce hardship. A party may have a meritorious counterclaim, set-off or cross-demand and may not raise it in the context of the CCA or by means of separate proceedings. Yet that party may be precluded from raising it in an application to set aside a bankruptcy notice or a statutory demand that follows an unsatisfied judgment issued under s 74. This seems hard. But while the adoption of the alternative view would alleviate this hardship, it would, as we have said, create another hardship – it would keep the party in whose favour the adjudicator had ruled from its entitlement under the CCA, and thereby frustrate its purpose."

[16] Mr O'Connor, for Herbert attempts to argue however that the Construction Contracts Act 2002 does not apply here, as Tuck failed to serve a valid payment claim in accordance with s 20 of that Act.

[17] Section 20 provides (as relevant):

> **20 Payment claims**
>
> (1) A payee may serve a payment claim on the payer for each progress payment,—
>
> (a) if the contract provides for the matter, at the end of the relevant period that is specified in, or is determined in accordance with the terms of, the contract; or
>
> (b) if the contract does not provide for the matter, at the end of the relevant period referred to in section 17(2).
>
> (2) A payment claim must—
>
> (a) be in writing; and
>
> (b) contain sufficient details to identify the construction contract to which the progress payment relates; and
>
> (c) identify the construction work and the relevant period to which the progress payment relates; and
>
> (d) indicate a claimed amount and the due date for payment; and
>
> (e) indicate the manner in which the payee calculated the claimed amount; and
>
> (f) state that it is made under this Act.
>
> ...

[18] On 24 July 2009 Mr Elmes, Tuck's manager, sent an email to Herbert which said:

> Hi Trish
>
> Please find attached our progress claim for the month up to 25th July. I will arrange invoicing with Beth when she returns next week.

[19] Attached to that email was a table itemising the amount owed to Tuck ($30,076.20). It seems, however, that no indication was given of the due date for payment and the claim is not specifically stated as being made under the Construction Contracts Act 2002.

[20] By invoice dated 28 July 2009, Tuck also invoiced Herbert for the $30,076.20 which figure was said to have arisen out of the job described as "CLAIM 3 AS ATTACHED CLAIM (EMAILED)". The attached claim was a copy of the table emailed on 24 July 2009. The invoice makes no mention of the claim being a "progress claim" but at the bottom of the invoice is the following:

> Please note that this invoice is due for payment on or before the 20/08/2009
> In Accordance with the Construction Contracts Act 2002

[21] Mr Gilmour, for Tuck, argues that to require a payment claim to include the express words "payment claim" is overly pedantic. Mr Gilmour bases that submission on the fact that no such words are contained in s 20 and further the Court of Appeal's decision in *George Developments Limited v Canam Construction Limited* [2006] 1 NZLR 177 requires that: (at [43])

> technical quibbles should not be allowed to vitiate a payment claim that substantively complies with the requirements of the Act…

[22] Section 3 of the Construction Contracts Act provides:

> **3 Purpose**
>
> The purpose of this Act is to reform the law relating to construction contracts, and, in particular –
>
> (a) to facilitate regular and timely payments between the parties to a construction contract; and
>
> (b) to provide for the speedy resolution of disputes arising under a construction contract; and
>
> (c) to provide remedies for the recovery of payments under a construction contract.

[23] In considering this general purpose, the Court of Appeal in *George Developments Limited v Canam Construction Limited* [2006] 1 NZLR 177 stated at [31]:

> The purpose provision of the Act includes the fact that the Act was 'to facilitate regular and timely payments between the parties to a construction contract'. The importance of such regular and timely payments is well recognised. Lord Denning (quoted in *Gilbert-Ash (Northern) Ltd v Modern Engineering (Bristol) Ltd* [1973] 3 All ER 195, 214 (HL) Lord Diplock) said: 'There must be a 'cashflow' in the building trade. It is the very life blood of the enterprise'.

[24] And, in *Salem Ltd v Top End Homes Ltd* (2005) 18 PRNZ 122 the Court of Appeal again reiterated this at [11]:

> The whole thrust of the Act is to ensure that disputes are dealt with promptly and payments made promptly, because of the disastrous effects that non-payment has, not only on the head contractor, but also on its employees, subcontractors, and suppliers: *George Developments Ltd v Canam Construction Ltd* CA244/04 12 April 2005 at [41]-[42]. It is relevant to note, for instance, that employers cannot set up counterclaims, set-offs, or cross demands as a bar to the recovery of a debt under s23 of the Act, unless the employer has a judgment in respect of its claim or there is not in fact any dispute between the parties in relation to the employer's claim: s79. The fundamental position under the Act is that, if a progress claim is made and the employer does not respond within the period stipulated in the construction contract or, by default, within the time specified in the Act, the amount of the claim becomes payable forthwith.

[25] In the present case it is evident that this was a payment claim. Materially the same invoice had been sent by way of email days earlier. I consider this to be a mere technical quibble. Therefore, I find that a valid payment claim was served on Herbert. Herbert having failed to respond by delivering a payment schedule to Tuck is therefore at the mercy of ss 22 and 23 of the Construction Contracts Act 2002. I am satisfied therefore that in terms of ss 22 and 23, the unpaid balance of Tuck's claim issued by invoice in relation to the services rendered at the Hawke's Bay Airport, constitutes a debt due under the Construction Contracts Act 2002 and Herbert is liable to pay that amount.

[26] That same analysis applies with regard to the invoice in relation to the Guardian Trust building, Tuck having issued the same form of invoice in that matter (ie one where the words "payment claim" were not expressly recorded).

[27] With regard to the Guardian Trust building, Herbert does not contend that the amount is withheld due to any dispute in relation to the claim for the amount itself. Rather Herbert alleges that it has a valid cross-claim. In circumstances where s 79 of the Construction Contracts Act 2002 disallows any counterclaim, set-off or cross-demand and s 79 overrides the Companies Act 1993, I cannot set-aside the statutory demand with regard to Herbert's liability to Tuck for the work undertaken at the Guardian Trust building. If Herbert incurs liability for remedial works to the concrete in the Guardian Trust building it must bring an action against Tuck, although I acknowledge that Tuck is in liquidation and accordingly may be unlikely to be able to pay.

[28] With regard to the work at Hawke's Bay Airport, Mr Gilmour for Tuck argues that Herbert cannot avoid liability for payment. He submits that once it is established that the scheme of the Construction Contracts Act 2002 applies, Herbert is liable. In that submission, Mr Gilmour relied on a statement of mine in *Luxta Limited v Capital Construction Limited* (2010) 19 PRNZ 678 at [19]:

> The regime under the CCA establishes an obligation to pay for a payment claim, unless the principal (in this case Luxta) issues a payment schedule within the required time-frame, regardless of whether the claim is disputed.

[29] First, that case is distinguishable from the present in that in *Luxta*, the applicant's sole argument for setting aside the statutory demand was that the use of a statutory demand was an abuse of process.

[30] Secondly, despite s 79 of the Construction Contracts Act, however, it is perhaps arguable that if there is, in fact, a real dispute between the parties in relation to the claim for

the specific amount in question, Herbert may, in any event, be able to avail itself of some remedy under the Construction Contracts Act 2002.

[31] Turning to this aspect, Herbert does argue here that there is a substantial dispute between the parties in the present case, and this relates to allegations that Tuck did not perform its obligations under its contract with Herbert to the standard required under the Structural Specifications required under Herbert's contract with Skyline Aviation Ltd. Herbert claims that Tuck, in breach of those specifications, failed to use concrete from an accredited cement manufacturer and then failed to provide a testing report for the concrete. Herbert further claims that there is now cracking in the concrete taxiway and some of that cracking is structural.

[32] For two reasons I consider that these cannot be grounds here to claim that there is a dispute in relation to the claim. First, it is not clear under the contract between Tuck and Herbert whether Tuck must ensure that it adheres to the standards. The only mention in the contract to the standards is under the "SPECIAL CONDITIONS OF CONTRACT":

> It is your [Tuck's] responsibility to now familiarize yourself with Contract Specifications, if you have not already done so. A copy is always available at this office.

[33] Secondly, while Mr Herbert deposes that Herbert did not receive a copy of the certificate of practical completion, and one was not presented before me in related proceedings (*Herbert Construction Company Limited v Toogood* HC Napier CIV-2010-441-283, 20 August 2010), it seems one was certainly issued in 2009. Accordingly, the maintenance period ended in November 2009. Therefore, any liability that Herbert might have for cracking in the taxiway which arises subsequent to November 2009 if, for example, the concrete did not meet contractual standards, is unlikely to affect whether the present payment claim is due to Tuck under the Construction Contracts Act 2002.

[34] Mr O'Connor for Herbert further argues that as a final certification has not been issued under the Head Contract by the architect, the retentions withheld under the contract between Tuck and Herbert are not required to be released. Under the "SPECIAL CONDITIONS OF CONTRACT" between Tuck and Herbert:

- **Retentions of 10% will be held on this Contract**
- The release of retentions will only be made following final certification from the Architect.

[35] I accept that final certification from the architect under the Head Contract has not been forthcoming. However, it appears that final certification will never be forthcoming.

Further, as deposed before me by Mr Barrett, one of Tuck's liquidator accountants, an architect was not involved with this part of the project. The person likely to sign off any certification was the engineer, Mr Nettlington. While I accept that he has not done so, I consider that there are three reasons why the claim may not be avoided for purported retentions being withheld.

[36] First, it appears Herbert has received payment under the Head Contract for its construction work. I accept that payment may not have been in full, but following proceedings before me in *Herbert Construction Company Limited v Toogood* it seems Herbert and Mr Toogood the developer/owner settled all claims before this Court for $55,000. Those claims related to unpaid invoices which Herbert had delivered to Mr Toogood, but remained unpaid. Mr Herbert deposed that the parties settled as I declined to award summary judgment to Herbert for the $71,522.06 claimed in those proceedings on the basis that a certificate of practical completion had not been issued. In hindsight, it seems it had. However, whether Herbert wishes to pursue those matters against Mr Toogood is a matter for it. The result of those proceedings and subsequent settlement is that Herbert has received payment for its work. In that light, I do not consider that it can reasonably argue that it can withhold funds for work done by Tuck on the basis that the contract has allegedly not been completed. The purpose of retentions is to withhold funds in the event that immediate faults become apparent or maintenance become necessary. The project as far as the developers/owners are concerned is complete and as a result, Herbert faces no liability in that regard. For Herbert to now be able to hold on to retained funds, perhaps indefinitely, creates a nonsense of the commercial reality between the parties in circumstances where Tuck has no control over whether or not Mr Toogood may engage someone to produce a final certification of the works.

[37] Secondly, as deposed by Mr Barrett in his 29 March 2011 affidavit, it appears that the monies withheld are not strictly retentions when one looks at Herbert's pattern of payment. The invoice sent on 28 July 2009 (for $30,076.20) was the fourth in Tuck's series of invoices to Herbert for work on the airport site. Tuck received part payment of $7,785.40 on 21 August 2009. Tuck delivered a further invoice to Herbert on 31 August 2009 claiming payment of $10,676.76. That invoice was paid in full in two instalments on 22 December 2009 and 4 February 2010. Given the fact that part of the 28 July 2009 invoice was paid and subsequent payments were made, this suggests that the withholding of payment was not strictly for retentions. Further, from Tuck's last payment table it billed Herbert $194,468.38 for work in total. $22,290.80 is somewhat more than 10 per cent of that figure.

[38] Thirdly, in any event, there does not appear to be any issue taken now with the state of the work completed by Tuck or Herbert. Mr Toogood, Skyline Aviation Ltd's managing director deposes in his affidavit at paragraph 7 that:

> given that the defects identified and referred to with the practical completion certificate have been attended to, Skyline is content that all work required of Tuck as Herbert's sub-contractor, have been attended to to Skyline's satisfaction.

[39] And, Mr Sutton, the Hawke's Bay Airport Authority's general manager, deposes at paragraph 9:

> The Airport Authority has paid for the work carried out in full and is quite happy with the workmanship.

[40] For those reasons, I am satisfied that there can be no real dispute here between the parties in relation to the present claim by Tuck.

[41] And the issue of Herbert's solvency is not relevant under the present circumstances to the application before me, although it will of course take on significance if this matter needs to proceed to a full liquidation application.

Conclusion

[42] For all the reasons outlined above, the application before me is dismissed and accordingly, I decline to set-aside the statutory demand. Herbert is to have a further ten (10) working days from the date of this judgment to comply with the statutory demand, failing which a liquidation application may be brought.

[43] Tuck having been successful before me, I consider that it is entitled to costs. I note that Mr Gilmour seeks the opportunity to provide information in support of a costs claim. I accordingly invite the parties to file memoranda sequentially with regard to the question of costs which are to be referred to me for a decision.

'Associate Judge D.I. Gendall'