

#27

**IN THE HIGH COURT OF NEW ZEALAND
WHANGAREI REGISTRY**

CIV-2006-488-645

UNDER the District Courts Act 1947
IN THE MATTER OF an appeal against a judgment of the District
Court at Dargaville dated 6 September
2006
BETWEEN METALCRAFT INDUSTRIES LTD
Plaintiff
AND LINDA CHRISTIE
Defendant

Hearing: 9 February 2007

Appearances: Andrew Hazelton for Appellant
Gregory Clarke for Respondent

Judgment: 15 February 2007

JUDGMENT OF HARRISON J

*In accordance with R540(4) I direct that the Registrar
endorse this judgment with the delivery time of
2.30 pm on 15 February 2007*

SOLICITORS

Hazelton Law (Wellington) for Appellant
Pegg Ayton Gordon (Dargaville) for Respondent

Introduction

[1] This appeal by a contractor against a decision in the District Court refusing to enter summary judgment against its principal raises one discrete issue.

[2] The question is whether a letter sent by the principal's solicitor in response to the contractor's payment claim constitutes a payment schedule within the meaning of s 21(3) Construction Contracts Act 2002. If so, it was sufficient to justify the principal withholding payment on the contractor's claim; if not, the claim constitutes a debt enforceable in the District Court: ss 22 and 23.

District Court

[3] The relevant facts and statutory provisions are set out with clarity in Judge Keith de Ridder's decision delivered in the District Court at Dargaville on 6 September 2006. As a result it is only necessary for me to provide a truncated summary of the background circumstances.

[4] Ms Linda Christie owns a property at Ruawai, near Dargaville. On 20 June 2005 she accepted a written quotation from Metalcraft Industries Ltd to install a new roof on her dwelling for the sum of \$8252 plus GST. It is now common ground that the provisions of the Construction Contracts Act governed the contractual relationship: ss 5, 6, 9, 10 and 12.

[5] A dispute arose between the parties about the quality of Metalcraft's work performed through a subcontractor in July 2005. On 9 August Ms Christie's solicitors, Pegg Ayton Gordon, wrote to Metalcraft summarising the nature of her complaints in these terms:

We had received instructions from Ms Christie last week and as a result of that she made contact with your company giving your company a final opportunity to complete her roofing job which was supposed to be undertaken early June this year. Our client is appalled and distressed by the delays in this matter not least the initial poor workmanship which led to significant leaking and water damage to her home. After assurances from your company she was prepared to give a final opportunity for your company to honour its side of the contract and attend to the work. We

understand one and a half days' work was done following our client's recent complaint, last week, however, no-one showed up Monday this week or today. Our client received a call from Mr Comber's labourer, a 'courtesy' call, last night explaining that they had not attended the job because of wet weather.

Yesterday the weather was fine in Ruawai and the job could have been attended to.

The conduct of your company, the broken promises, the delays, the poor workmanship, have already led to our client being hospitalised by the stress caused to her. She is unwell, suffers from a terminal illness and is not able to tolerate any further delays or problems.

We give, on behalf of our client, this formal and final ultimatum. If your company does not arrange for suitably qualified roofers to attend our client's property tomorrow, 10 August 2005, and then continuously during normal working hours until the job is completed, their being absent only with our client's prior written consent given through this office, the contract will be cancelled, due to the ongoing serious and fundamental breaches.

If our client is forced to cancel the contract she will be hiring another available and suitably qualified roofer, and will be deducting the costs of that contract, and her expenses to date from the sum contracted for completion of the work.

If our client is forced to take these steps it is likely proceedings will issue for the recovery of any excess losses incurred by our client, and for the damage caused by your contractors to date, which have been the subject of two, as yet unresolved, insurance claims.

[6] The following day Pegg Ayton gave notice of cancellation of the contract on Ms Christie's behalf. Metalcraft rejected the notice, but later cancelled on 31 August following Pegg Ayton's advice that Ms Christie had '... arranged an independent contractor to complete the work and this has predominantly been completed'.

[7] On 31 August Metalcraft issued its one and only payment claim for the full amount of the contract price of \$8252, less a deduction for works not completed being 27 hours of labour worth \$540: s 20(2). Its net claim was for \$7712. Ms Christie challenged the document's validity as a discrete ground of defence to Metalcraft's claim for summary judgment. However, Judge de Ridder was satisfied that it constituted a valid claim. Ms Christie has not cross-appealed against his finding and I do not need to consider this issue further.

[8] Ms Christie had 20 working days to provide a payment schedule from the date of receipt of the payment claim: s 22(b)(ii). On 23 September Pegg Ayton wrote to Metalcraft's solicitors as follows:

... In any event our client disputes liability for payment, and advises that she is unable to specify if any payment is to be made to your client until she receives invoices for the remedial work undertaken by her replacement contractors. This, and our earlier correspondence, is to be regarded as our client's reasons for withholding payment. The cost of the remedial work is expected to exceed your client's invoice.

... Any summary judgment proceeding on the basis of your claim that the sum is a debt due, or otherwise, will be defended and costs will be sought.

[9] The Judge was satisfied that this letter constituted a payment schedule: s 21(2) and (3). He concluded that the letter indicated a scheduled amount of nil: ss 19 and 21(2)(c), together with an explanation of the manner of its calculation, Ms Christie's reasons for the difference between the scheduled amount and the claim, and her reasons for withholding payment. Accordingly, there was no debt due and he dismissed Metalcraft's claim for summary judgment.

Decision

[10] Metalcraft has appealed on the ground that Judge de Ridder erred in finding that Pegg Ayton's letter was a valid payment schedule.

[11] The Construction Contracts Act is a remedial measure. Its purpose is: s 3:

... 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.

[My emphasis]

[12] The Court of Appeal has recently emphasised the necessity of analysing disputes under the Act with its purposes in mind: *George Developments Ltd v*

Canam Construction Ltd [2006] 1 NZLR 177, noting the particular importance of cashflow in the building trade as ‘the very life blood of the enterprise’: at [41]. Like Judge de Ridder, I respectfully endorse and adopt Asher J’s overview of the statute’s objectives: *Marsden Villas Ltd v Wooding Construction Ltd*, HC Auckland CIV-2006-404-002136 25 May 2006:

[16] The Act sets up a procedure whereby requests for payment are to be provided by contractors in a certain form. They must be responded to by the principal within a certain timeframe and in a certain form, failing which the amount claimed by the contractor will become due for payment and can be enforced in the Courts as a debt. At that point, if the principal has failed to provide the response within the necessary time frame, the payment claimed must be made. **The substantive issues relating to the payment can still be argued at a later point and adjustments made later if it is shown that there was a set-off or other basis for reducing the contractor’s claim.** When there is a failure to pay the Act gives the contractor the right to give notice of intention to suspend work, and then if no payment is made, to suspend work. There is also a procedure set up for the adjudication of disputes.

[17] The Act therefore has a focus on a payment procedure, the results that arise from the observance or non-observance of those procedures, and the quick resolution of disputes. **The processes that it sets up are designed to side-step immediate engagement on the substantive issues such as set-off for poor workmanship which were in the past so often used as tools for unscrupulous principals and head contractors to delay payments.** As far as the principal is concerned, the regime set up is ‘sudden death’. Should the principal not follow the correct procedure, it can be obliged to pay in the interim what is claimed, whatever the merits. In that way if a principal does not act in accordance with the quick procedures of the Act, that principal, rather than the contractor and sub-contractors, will have to bear the consequences of delay in terms of cashflow.

[My emphasis]

I shall return to the emphasised passages later in this judgment.

[13] The relevant requirements for a payment schedule are as follows: s 21:

- (1) A payer may respond to a payment claim by providing a payment schedule to the payee.
- (2) A payment schedule must—
 - (a) be in writing; and
 - (b) identify the payment claim to which it relates; and
 - (c) indicate a scheduled amount.

(3) If the scheduled amount is less than the claimed amount, the payment schedule must indicate—

- (a) the manner in which the payer calculated the scheduled amount; and
- (b) the payer's reason or reasons for the difference between the scheduled amount and the claimed amount; and
- (c) in a case where the difference is because the payer is withholding payment on any basis, the payer's reason or reasons for withholding payment.

[14] A 'scheduled amount' is defined as: s 19:

... an amount of progress payment specified in a payment schedule that the payer proposes to pay to the payee in response to a payment claim.

[15] I agree with Mr Andrew Hazelton, Metalcraft's counsel; the whole thrust of the payment claims provision in Part 2 is to enhance a contractor's entitlement to make and enforce progress claims unless they are properly disputed in a timely manner: *West City Construction Ltd v Edney*, HC Auckland CIV-2005-404-001066 1 July 2005, Venning J: at [44]. The specific purpose of the payment schedule is to give the contractor full and unequivocal notice of all areas of difference or dispute to enable it to properly assess its future options.

[16] In the circumstances of this case, three alternative courses were available to Metalcraft upon receipt of a valid payment schedule from Ms Christie: (1) to accept the reasons given for non-payment of the disputed amount, and to arrange to remedy or rectify the work if that remained possible or to abandon its claim; (2) to accept the letter as a bona fide notice of dispute, with sufficient identification of the grounds to refer the issue to adjudication under Part 3; or (3) to treat the letter as invalid or defective, and rely upon it as an admission of a debt giving rise to a right to claim summary judgment. Quantification of the monetary difference between the parties would be central to this exercise.

[17] Judge de Ridder found that Pegg Ayton's letter constituted a valid payment schedule on two grounds. First, he was satisfied that the letter indicated a scheduled amount of nil; it was 'the only sensible interpretation' available from it: at [35]. He accepted that:

[39] The facsimile of 23 September 2005 does not set out any arithmetical manner of calculation. However, it does refer to remedial work being undertaken by Ms Christie's own contractors and that the cost of remedial work is expected to exceed the payment claim. That is, in a sense, the manner in which the scheduled amount has been calculated. It also amounts to Ms Christie's reasons for the difference between the scheduled amount and the claimed amount.

[18] With respect, I disagree. In my judgment the letter, even when read in conjunction with earlier correspondence, does not approach satisfaction of the statutory requirements. It cannot be construed as indicating a scheduled amount of nil. To the contrary, Pegg Ayton specifically stated that Ms Christie was not then in a position 'to specify if any payment is to be made'. It was not an unequivocal denial of liability for all of the payment claim but was instead notice that Ms Christie would review her position at a later date. The strict provisions of Part 2 were enacted to pre-empt this very mischief.

[19] The statute does not allow for any delay in indicating a scheduled amount outside the specified time limit of 20 working days. A statement that Ms Christie 'is unable to specify if any payment is to be made ... until she receives invoices for the remedial work ...' could not justify a failure within that period to quantify the scheduled amount. Ms Christie could have discharged this obligation if she so wished. On 30 August Pegg Ayton had advised Metalcraft that the independent contractor whom Ms Christie had engaged following cancellation of the first contract had 'predominantly' completed remedial work. If that was so, it was simply a matter of Ms Christie providing proper details of the work and the independent contractor's charges, whether provisional or final. It would then be quantified as the amount to be reduced from Metalcraft's claim on account of faulty workmanship, assuming for these purposes that this would provide a valid reason for withholding payment of the balance, constituting the difference between the payment claim and scheduled amount.

[20] The direct consequence of the Judge's finding that the correspondence indicated a scheduled amount of nil was that Ms Christie was refusing to pay any or all of the contract price less a unilateral deduction offered by Metalcraft. She was asserting that nothing was owing despite the common ground that some work was carried out pursuant to the contract. Adoption of this position was extreme. That is

why in September 2005 Ms Christie was under a strict onus to explain with some precision the basis for calculating that Metalcraft was not then entitled to any payment.

[21] Ms Christie's statement of defence illustrates the invalidity of her payment schedule. She claims by way of set-off or counterclaim the sum of \$24,946. The bulk of the claim is unrelated to the Metalcraft payment claim, being for general damages, legal costs and the like, to a total of \$19,000, which could never succeed. Remedial expenditure amounts to about \$3500. For the first time, she quantified her denial of Metalcraft's claim for labour to install guttering at \$1756. Plainly this information should have been given in the payment schedule. The total of the two items is about \$5250, significantly below Metalcraft's claim of \$7712. This pleading constitutes Ms Christie's admission that on 31 August 2005 Metalcraft's valid payment claim was at least \$2500.

[22] Second, the Judge concluded that the letter validly indicated Ms Christie's reasons for the difference between the scheduled amount of nil and the amount claimed. He held:

[40] Finally, as the facsimile makes it clear that Ms Christie is withholding payment, she is required to provide reasons for that. The reasons given are that she considers remedial work is required and that the cost of that would exceed the payment claim. The facsimile also refers to previous correspondence as being reasons for withholding payment. Between 9 August 2005 and 23 September 2005 there were eight items of correspondence between Ms Christie's lawyers and Metalcraft or Metalcraft's lawyers. The letters from Ms Christie's lawyer referred to delays in completing the work, excess materials being supplied, initial poor workmanship leading to significant leaking and water damage to her home, and advising that if Metalcraft's obligations were not attended to in a timely manner she would cancel the contract and claim the costs of having her own contract to complete the work. The facsimile of 23 September confirms that Ms Christie had engaged her own contractors to complete the work.

[23] Again I respectfully disagree. An assertion that remedial work is required at a cost which would exceed the payment claim could never constitute a valid reason either for the difference between the scheduled amount and the amount claimed or for withholding payment. General and unspecified allegations of defective workmanship are insufficient unless quantified within a reduction for the claimed cost of remedial work. Similarly a claim that excess materials were supplied is not

enough; Ms Christie would have to identify them and their value to justify a further reduction in the scheduled amount. Delays in completing the work and consequential damage caused by leaking and water damage may give rise to a counterclaim for special damages, but even if quantified they could not be taken into account in the scheduled amount: s 79. None of the reasons given in Pegg Ayton's correspondence justified withholding payment of any part of Metalcraft's claim.

[24] In a spirited defence of Judge de Ridder's decision, Mr Gregory Clarke, Ms Christie's counsel, sought salvation in *Westnorth Labour Hire Ltd v SB Properties Ltd* HC Auckland CIV-2006-404-001858 19 December 2006, Rodney Hansen J, dismissing an appeal from the District Court's finding that a lengthy letter from the principal constituted a payment schedule: at [6]. Rodney Hansen J held:

[28] Again I agree with the Judge. Although the letter does not adopt the terminology of the Act, is not stated to be a payment schedule and does not specify that the scheduled amount is nil, the essential message is clear and unequivocal. Mr Mullane explains why he now doubts the accuracy of Westnorth timesheets and hence the sums he has been charged. He identifies a charge for materials that have been returned and instances of faulty workmanship which would entitle S B Properties to counterclaim. He says he will not pay the two invoices until Westnorth provides him with full particulars of what the contracted labour has done.

[29] The relevant provisions of the New South Wales Building and Construction Industries Security of Payment Act 1999 are almost identical to the provisions of the New Zealand Act governing payment schedules. In the leading case of *Multiplex Constructions Pty Limited v Luikens* [2003] NSWSC 1140, the Court said at para [78]:

Section 14(3) of the Act, in requiring a respondent to 'indicate' its reasons for withholding payment, does not require that a payment schedule give full particulars of those reasons. The use of the word 'indicate' rather than 'state', 'specify' or 'set out', conveys an impression that some want of precision and particularity is permissible as long as the essence of 'the reason' for withholding payment is made known sufficiently to enable the claimant to make a decision whether or not to pursue the claim and to understand the nature of the case it will have to meet in an adjudication.

[30] In my judgment, the letter meets these basic requirements. Westnorth was given all the information it needed to understand S B Properties' position, to decide whether to pursue its claim and the case it would be required to meet at adjudication. I am satisfied the Judge was right to conclude that the letter was a payment schedule which complied with s 21 of the Act.

[25] With respect, *Westnorth* does not assist Ms Christie. Each case in this area largely depends upon the contents of the documents under consideration. In *Westnorth* Rodney Hansen J was satisfied, for good reason, that the principal's letter was valid. (I doubt that his reference to the prospect of a counterclaim was meant to recognise that this factor would justify non-payment). As Rodney Hansen J found, the principal's letter provided all the information necessary for the contractor to understand its position and make the appropriate consequential decisions. And as Mr Hazelton points out, the principal's correspondence in *Westnorth* contained a number of arithmetical calculations, beginning with the amount of the invoices, their relationship to projected budgets and total previous payments and figures for materials returned – in substance a calculation indicating why no money was considered to be then payable. Pegg Ayton's correspondence fell well short of that mark.

[26] As an afterthought, following his earlier acceptance of Asher J's summary of the purpose and reach of the Act in *Marsden Villas* at [16] and [17], Mr Clarke challenged Asher J's apparent view that the Act excluded claims of set-off from the legitimate ambit of a payment schedule. Before the statute was enacted, such claims were commonplace by principals and head contractors, operating to the detriment of the construction industry by perpetuating financial uncertainty. Withholding payments, often on a pretext or with little foundation, was a regular tactic designed to impose pressure on a contractor or sub-contractor to abandon or accept a significant reduction in its final claim for the advantage of finality. It was a means of freezing out a contractor who had neither the means nor appetite for litigation or arbitration.

[27] Parliament's remedial intention in its expression of the statute's purposes is reinforced by s 79. It provides that in any proceeding for a recovery of a debt under Part 2, the Court must not give effect to any counterclaim, set-off or cross-claim raised by a principal other than a set-off of a liquidated amount where either judgment has been entered for that amount or there is no dispute between the parties relating to the claim for it.

[28] Accordingly, a principal's denial of liability for a payment claim on the ground that a right of set-off exists will be insufficient. Nevertheless, a payment schedule which properly quantifies the amount incurred by a principal in remedying allegedly defective workmanship by a contractor may, in the particular circumstances of the case, constitute a valid reason for withholding payment for that amount. It may be accepted as the financial measure of the contractor's defective workmanship or materials amounting in law to a breach of contract for which it is not entitled to recover. If such circumstances exist, the contractor may be advised to proceed to adjudication with its associated strict timeframe rather than attempting to argue that a debt is now due and enforceable in a Court of law. However, that question does not arise for determination here given my primary conclusions.

[29] Accordingly, I allow Metalcraft's appeal and enter summary judgment for it against Ms Christie in the sum of \$7712.62 plus GST of \$964.08 and interest calculated at the rate of 7.5% from the date the proceeding was filed in the District Court. Metalcraft is also entitled to its actual and reasonable costs in the District Court and on appeal: s 59(2)(a)(ii).

Rhys Harrison J