FENWICK ELLIOTT

The construction & energy law specialists

Issue 212 - February 2018

Dispatch highlights some of the most important legal developments during the last month, relating to the building, engineering and energy sectors.

Dispatch

Adjudication: Part 8 and natural justice

Victory House General Partner Ltd v RGB P&C Ltd
[2018] EWHC 102 (TCC)

This was an adjudication enforcement case arising out of the development and conversion of an existing office building into a hotel in London. The employer, VH, brought a Part 8 claim, which was met by an application for summary judgment to enforce an adjudicator's decision by RGB.

Deputy Judge Smith QC did not consider that the case was suitable for a Part 8 application as it raised matters of disputed fact. The Part 8 procedure should only be used where a claimant seeks a court decision on a question which is unlikely to involve a substantial dispute of fact. It was not an answer to this point to suggest that issues could be resolved in the Part 8 proceedings on the basis of assumed facts. This would potentially result in the unsatisfactory situation where a party, if dissatisfied with the Part 8 decision, would still then be in a position to challenge any disputed matters of fact at a later time in further substantive proceedings. There would be no saving of costs and resources and no advantage in permitting determination of the issues to be expedited.

Under the contract, RGB was obliged to procure a transformer or substation. Until the transformer was installed, the electrical and mechanical services could not be completed. The project fell into delay and there was a disagreement about payment. In March 2017, the parties entered into a short Memorandum of Understanding ("MoU"). The MoU provided for three stage payments. The first two were made, VH said in accordance with the MoU, and it was common ground that the transformer was installed. The next month, RGB issued Application 30 in the sum of some £680k plus VAT. VH refused to pay this sum, saying that the payment terms were now governed by the MoU. RGB said that the payment notice was late, there was no pay less notice and, contending that the MoU was not binding, referred this dispute to adjudication. During the adjudication, RGB's position shifted to noting that whilst the MoU was legally binding the parties did not intend it to replace the provisions of the Contract.

Towards the end of the adjudication process, the Adjudicator asked a series of questions. Both parties replied. In the Decision, the Adjudicator rejected RGB's primary case that the MoU was not legally binding but also rejected VH's case that the MoU superseded the Contract and effectively governed what payments were to be made by VH to RGB up to the date of Practical Completion. Instead, the Adjudicator held that the true effect of the MoU was to suspend the obligation on VH to make interim payments under the Contract until such time as the transformer was installed. Given that Application 30 was made after that date, it was valid and, in the absence of any valid pay less notice, was payable. VH said that the Adjudicator's decision as to the true construction of the MoU did not reflect an argument that had been advanced by either party. The Adjudicator had invented a new point on construction which was central to his Decision and so was a material breach of natural justice.

The Judge disagreed. The parties were aware from the outset that a central question in the adjudication concerned the true and proper construction of the MoU. They each made detailed submissions on this issue. Echoing the words of Mr Justice Fraser in the case of *AECOM Design Build Ltd v Staptina Engineering Services Ltd* [2017] EWHC 723 (TCC), the Judge noted that a party wishing that they had put more comprehensive submissions to the adjudicator on the point he had highlighted was "not the same as there having been a breach of natural justice, still less a material breach". The Adjudicator did not go off on a frolic of his own. The Decision was made against the background of having posed a specific question about the purpose, scope and effect of the MoU and Contract; a question which both parties had the opportunity to answer.

Termination: getting the notice right

Phones 4U Ltd (in administration) v EE Ltd
[2018] EWHC 49 (Comm)

On 15 September 2014, Phones 4U appointed administrators and ceased to trade. On 17 September 2014, EE terminated the Trading Agreement ("TA"). Phones 4U subsequently made a claim for unpaid commission fees. By counterclaim, EE sought damages at common law alleging that in breach of its contractual obligations Phones 4U had failed to engage in its normal trading activities as authorised seller of EE products and services. EE said that this was a repudiatory breach of contract. Clause 14.1 of the TA gave either party the right at any time to terminate by giving notice in writing to the other with immediate effect:

"14.1.1 if the other party commits a material breach of this Agreement and either such breach is incapable of remedy or, if capable of remedy, has not been remedied to the reasonable satisfaction of the other party within 30 days of a written request from the other party to remedy such breach; or
14.1.2 if the other party is unable to pay its debts ... or takes any steps (or any third party takes any steps in respect of the other party) to: initiate a composition, scheme, or other arrangement with any of its creditors..."

It was common ground that the appointment of administrators over Phones 4U gave EE the right to terminate under clause 14.1.2, by giving notice in writing. It was also common ground that the appointment of administrators was not a breach of contract on the part of Phones 4U, and neither involved, nor inevitably resulted in, such a breach. Mr Justice Baker explained that in the termination notice:

(i) EE stated expressly that it was terminating with immediate effect;
(ii) EE also stated expressly that it was terminating pursuant to clause 14.1.2;
(iii) EE did not identify any breach of contract by Phones 4U as causing, justifying or having relevance to its decision to terminate, whether by asserting breach in terms or by referring to or asserting facts that were now said to have amounted to breach;
(iv) EE said that as a result of termination Phones 4U's authority to sell and promote EE products and services was also terminated.

There was a difference between terminating the contract as a result of the appointment of the administrators and then going on to allege at a later stage that Phones 4U were in breach of their obligation to market EE products. Whilst EE had expressly exercised their contractual right to terminate, at the time of termination no mention was made of any other breach (actual or anticipatory) even though in fact such a repudiatory breach and/or renunciation in fact existed. Phones 4U said that because the termination was solely made by reference to clause 14.1.2 of the TA, the counterclaim could not be brought. As this was an application for summary judgment, the court assumed that Phones 4U had breached the obligations alleged when it ceased trading.

The question for the court was whether it was necessary, for the common law claim for loss of bargain damages, that EE had terminated for breach (actual or anticipatory) by Phones 4U. Did EE have to show that the termination letter was an exercise of its common law right to terminate for repudiatory breach, and not simply a termination under clause 14.1.1 of the TA? Phones 4U said that this was what EE had to do and that EE had to communicate to Phones 4U that this was what it was doing. Further, Phones 4U said that the termination letter did not do this. The termination was independent of the breach now being alleged.

Mr Justice Baker agreed that in order to make their claim for loss of bargain damages, EE must show that the termination of the contract, which created the loss of bargain, resulted from a repudiatory breach by Phones 4U. Where a party terminated a contract in sole reliance on a contractual right to terminate without breach by the other party, it could not subsequently claim common law "loss of bargain" damages on the basis that it had terminated in response to the other party's repudiatory breach, even if there had been such a breach.

To bring such a claim, the terminating party had to clearly communicate that it was exercising its common law right to terminate for repudiatory breach. EE therefore had to show that the contract was terminated by its exercise of its common law right to terminate for that breach. The problem for EE was that the termination letter communicated only the contractual termination. It did not matter that EE could have terminated for other reasons; they did not. The Judge concluded that the termination letter:

"communicated unequivocally that EE was terminating in exercise of, and only of, its right to do so under clause 14.1.2, a right independent of any breach. Phones 4U was not accused of breach. EE made clear it was not to be taken as waiving any breach that might exist, any rights in respect of which were reserved. But a right merely reserved is a right not exercised. EE can still sue upon any breach of contract committed by Phones 4U prior to termination. For any such breach, it may pursue all remedies that may be available to it bearing in mind that the contract was terminated under clause 14.1.2 and not for breach. But what EE cannot do is re-characterise the events after the fact and claim that it terminated for breach when that is simply not what it did. Nor can it say that it treated Phones 4U's renunciation (as now alleged) as bringing the contract to an end when that, again, is just not what actually happened."

Settlement agreements

Fluor Ltd v Shanghai Zhenhua Heavy Industry Co, Ltd

[2018] EWHC 1 (TCC)

The dispute here arose out of a contract for a 140 turbine wind farm in the North Sea. There were faults with the turbines supplied by SZH to Fluor. Fluor settled the claim up the line with CGOWL and sought to recover the settlement sums from SZH. Mr Justice Stuart-Smith recalled that:

"It is settled law that, in principle, C can recover from a contract breaker, B, sums that it has paid to A in settlement of a claim made by A against C in respect of loss caused by B's breach of its contract with C.

However, C's settlement with A must be an objectively reasonable settlement and, if it is, that sum represents the measure of C's damages in respect of B's breach of contract (assuming that there were no other heads of loss). Even if C can show that its settlement with A was at an undervalue, the settlement sum still represents a ceiling on the amount that it can recover from B."

The Judge noted that the position is more complicated where several heads of claim have been settled between an employer and a main contractor but where a defendant subcontractor is alleged to have been responsible for only one of them. This was not a case where Fluor refused to explain how the settlement sum was to be apportioned, but SZH did not accept the explanation given by Fluor. Amongst the questions the Judge had to consider were: what claims were actually settled by the payment made by Fluor, what amounts should be apportioned to them and how was that apportionment affected by the fact that Fluor sacrificed some other claims of its own? The approach of the Judge was to establish what proportion of the sum paid (or foregone) by Fluor was attributable to breaches of contract by SZH and, of those, what was in respect of costs or delays which had not been waived. Having established that, the court then had to consider whether or not that proportion of the settlement sum was reasonable. Here, Fluor had assumed a very substantial potential liability under a warranty, albeit the risk was thought to be low.

The Judge was of the view that Fluor's settlement was intended to embrace all claims relating to the project. Therefore it was necessary for the court to establish exactly what claims were "on the table" at the time of the settlement. When considering a global settlement the court was, in the words of the Judge "bound" to look at all the material available to it. This was a matter of elementary fairness. A third party should be liable only for the direct consequences of its breaches of contract, and not consequences that are the product - or said to be the product - of an agreement between two other parties into which it had no input. The Judge then considered the circumstances leading up to the settlement agreement. He identified which items were claims arising out of defects in the welds, which had not been compromised by a waiver letter. Of these, he concluded that:

"Overall, the settlement ... was the result of hard fought and protracted negotiations in which each side had the benefit of informed legal advice. None, or at least very few, of the claims to which a value had been attributed by either party was so weak as not to be taken seriously. The analysis that I have carried out shows that the reasonable settlement value of CGOWL's claims was very close to the sum paid or foregone by Fluor, so on that basis alone that aspect of the settlement was self-evidently reasonable."

Dispatch is produced monthly by Fenwick Elliott LLP, the leading specialist construction law firm in the UK, working with clients in the building, engineering and energy sectors throughout the world.

Dispatch is a newsletter and does not provide legal advice.

Edited by **Jeremy Glover, Partner**
jglover@fenwickelliott.com
Tel: + 44 (0)20 7421 1986

Fenwick Elliott LLP
Aldwych House
71 - 91 Aldwych
London WC2B 4HN