



Fenwick Elliott

The construction & energy law specialists

# Annual Review

A round-up of key developments in the construction, engineering and energy arena



## 2012/2013

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Bringing clarity to the drafting of commercial contracts

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The legal and contractual implications of BIM

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Global claims in practice: what do you need to prove?

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The consequences of failing to mediate: an update

## ANNUAL REVIEW 2012/2013

Fenwick Elliott is the UK's largest specialist construction law firm with clients across the world. We advise on every aspect of the construction process in the building, engineering and energy sectors, including oil, gas, nuclear and power.

Our expertise includes procurement strategy, contract documentation and negotiation, risk management and dispute avoidance, project support, and decisive dispute resolution, including international arbitration, mediation and adjudication.

Our approach is commercial. We aim to add value to transactions and find practical solutions to disputes.



**Fenwick Elliott**  
The construction & energy law specialists

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**Simon Tolson**  
Senior partner

## First word

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*It is my great pleasure to introduce the 2012/13 edition of the Fenwick Elliott Annual Review. This is our 16th such annual publication, and it is always great fun to try to squeeze in to one journal the highlights of the wider legal year. Our purpose is to be informative and to alert you to areas of the law and practice which may be relevant to your business endeavours. We recognise that while you need to make sure you avoid getting on the wrong side of the contract or the law, keeping up with the latest developments and staying ahead of the pack is just one thing in a long list of tasks you need to fit in to your busy day. The Review allows you to sit down and 'catch up'.*

Once again our Review has an international feel, for Fenwick Elliott is a truly international construction law business. However, our dominance in the legal construction and energy law market here at home remains at the top of the tree, and rightly nurtured. London is still our engine room; we all just travel a lot more these days. I am pleased to say it has been a year vibrant with plenty of action; in fact it has been the busiest year that I can recall in 25 plus years at the firm. The firm has expanded significantly, there are new faces and we have now out grown our first floor plate at Aldwych House, moving some of the team on to the 8th floor.

Our range of construction and energy work is now immense. The types of work includes wind turbine disputes, highways, mega-skyscrapers, process plants of every description, airports, tunnelling, subsea structures, pipelines, bridge deck failures, well head projects and deep basements. You name it, we are on something exciting and/or muddy. We are also working with pretty well every English language-based construction contract in use, and of course many are bespoke.

Our work continues to cover dispute avoidance strategy, litigation, international arbitration, adjudication and all forms of ADR. Our projects team have also been so busy that we have expanded the unit again this year. That can only mean the food chain in development work in London (and we sense elsewhere) is cranking up. Our remodelled website now does justice to who we are and what we do and if you want to keep track of our latest legal updates you can now follow us on Twitter or LinkedIn.

We are doing very nicely reputationally in our central London position whether for our commercial legal work, or for dispute resolution through litigation, arbitration or mediation. London too is a global leader in commercial dispute resolution. English judgments are easily enforceable, not simply within the EU but also in most parts of the world, even when there are no reciprocal enforcement arrangements.

Our judges have reputations for excellence, robustness, integrity and yes, honesty. In general, newly-appointed TCC judges in England have had 30 years' experience as practitioners, arguing cases of the variety that they will now have to resolve judicially. This is one reason why our TCC judges are held in such high regard. They know a thing or two about bonding, retention, tensile forces and checkerplate.

Our experts' pool is also amongst the very best in the world, experienced in all the fields in which disputes arise, including mechanical and civil engineers, forensic accountants, scientists from every discipline, oil and gas technologists, specialists in computer hardware and software and yes, delay experts.

We have also now run a number of cases in the new Rolls Building, which as some of you know, is the latest court to be constructed in the City. As a centre of excellence, it now takes its place alongside another of the City's world-famous seats of justice - the Old Bailey. It has already graced many international cases such as *Berezovsky v Abramovich* and yes, we have had to jostle with Roman Abramovich's body guard to get our papers into court!

We thank you, our clients, for the opportunity your problems have given us to resolve. Long may this continue to our mutual advantage!

**Simon J A Tolson**



**Jeremy Glover**

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Partner

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Editor

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## In this issue

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*Welcome to the sixteenth edition of our Annual Review. As always, our Review contains a round-up of some of the most important developments from the past 12 months including from page 40, our customary summaries - of some of the key legal cases and issues, taken from both our monthly newsletter Dispatch as well as the Construction Industry Law Letter.*

We have also right at the end of the *Review* included a copy of one of our recent newsletters, *Insight*, which takes a practical look at what the latest legal developments might mean for you. If you would like to know more, or to receive a monthly electronic copy, please contact Lisa Kingston, the editor. The issue to be found at pages 51-52 discusses how project bank accounts work in practice.

*Insight* is not our newest publication, however. In 2012 we introduced *International Quarterly* ("IQ"), which looks at legal and commercial developments in construction and energy sectors around the world. Our lead article in this year's *Review*, on pages 3-4, where Richard Smellie considers the impact of the *Rainy Sky* decision on the drafting and interpreting of contracts, was taken from the Summer edition of IQ. If you would like to receive a copy by email, please let me know.

Continuing the international theme, at pages 5-7 Frederic Gillion considers the impact of the new ICC rules of arbitration on construction disputes, whilst David Robertson on pages 24-25 looks at two decisions with their origins in India which are of importance when it comes to trying to enforce arbitral awards, wherever your project may be.

Many of our articles in this year's *Review* relate to matters of interest to both domestic and international contracts. Nicholas Gould, on pages 26-27, provides a helpful summary of some of the key principles relating to bonds and guarantees arising from recent court cases. And one of those "bond" cases, which we discuss on pages 28-29, provides some important lessons of the care needed when sending emails.

Developments in Building Information Modelling (BIM) carry on apace. On pages 16-18, Stacy Sinclair updates us on what we need to know, focusing on the legal and contractual implications.

We also round-up, on pages 21-24, some of the latest developments surrounding the EU Procurement Regulations. It is clear that the 30-day limit for bringing claims will be strictly enforced, and recently the courts have also been looking at the circumstances in which contracting authorities can seek clarifications of tenders and/or prospective tenderers can include a caveat with their bids.

Mediation remains an important consideration. The Court of Appeal has introduced a new mediation scheme for claims with a value of under £100,000. At pages 13-15, we look at some of the latest case law involving projects ranging from a hydroelectric generating plant in Brazil, to the meaning of repairing covenants of underleases relating to three floors of a building in London.

At pages 36-38, we review some of the distinctions between clauses which require that you use best or reasonable endeavours, or even all reasonable endeavours. It will come as no surprise that the only sure way to achieve certainty is clarity of drafting.

We are also excited that the *Fenwick Elliott Dictionary of Construction Terms*, the product of over 25 years experience, goes to print at the same time as the *Review*. See a small extract on page 39.

And sometimes, just sometimes, a case comes along which becomes compulsory reading. Mr Justice Akenhead's decision in the *Mackay* case, described as "a full-blooded conflict", provides an invaluable commentary on the principles involved in bringing delay and loss and/or expense claims. We look further at this on pages 30-33.

As always, I'd welcome any comments you may have on this year's *Review*. Just email me at [jglover@fenwickelliott.com](mailto:jglover@fenwickelliott.com).

**Jeremy Glover**

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## Contract interpretation

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# Contract interpretation: commercial intent takes centre stage

*Throughout the commercial world, on a daily basis, contracts, drawn up to regulate the commercial activities of parties to a business enterprise, are subjected to close scrutiny for the purpose of ascertaining legal rights and obligations. As Richard Smellie explains, where the language is clear, the rights and obligations will be clear, but language is often susceptible to more than one possible meaning, particularly when arguments arise or the unexpected occurs. The commercial world of international construction contracts is no exception. These contracts are often complex, and ascertaining the true nature of the parties' agreement on a particular point can be challenging.*

The starting point is, of course, the words on the page, but where there is conflict or ambiguity - as there often is when a dispute arises - they must be interpreted. It is at this point that the law of the contract steps in, with rules on how the contract is to be interpreted.

In English law, for many years now, there has been a steady move away from the application of individual, strict rules of interpretation, particularly for commercial contracts, with the primary touchstones being that the relevant provision in the contract must be interpreted in the context of the document as a whole, and that what the parties meant by the language used involves ascertaining what a reasonable person would have understood the parties to have meant.

To that end, the "reasonable person" is a person with the background knowledge that would have reasonably been available to the parties at the time they entered into the contract. However this definition excludes the subjective knowledge and intentions of the parties, and importantly excludes the detail of contract negotiations.

Recently, English law took a further, important step along the road of contract interpretation, in the decision of the Supreme Court in *Rainy Sky S.A. and Others v Kookmin Bank*. In short, the Supreme Court (which since October 2009 has been the highest court in the United Kingdom, taking over the judicial functions of the House of Lords) confirmed the particular importance of giving weight to "business common sense" in ascertaining what the parties meant by the language they used, when ambiguity arises.

The *Rainy Sky* decision concerned the insolvency of a shipbuilder, and whether the purchasers of vessels not completed at the time of the shipbuilder's insolvency could claim back monies paid to the shipbuilder against refund guarantees issued by the Kookmin Bank. The underlying shipbuilding contract provided that insolvency triggered the repayment of any advance instalments paid to the Buyers. However, although the guarantees recorded that the advance payments were repayable on certain conditions, they did not specify insolvency as one such ground.

This left a problem for the parties with the wording of the guarantees being open to two possible interpretations. The bank contended for a literal interpretation, which, whilst making the guarantees available for many types of default by the shipbuilder, meant that the guarantees were not available as security in the event of the shipbuilder's insolvency.

The bank succeeded on its interpretation before the Court of Appeal. In particular the Court of Appeal said as follows:

*"Unless the most natural meaning of the words produces a result which is so extreme as to suggest that it was unintended, the court has no alternative but to give effect to its terms. To do otherwise would be to risk imposing obligations on one or other party which they were never willing to assume and in circumstances which amount to no more than guesswork on the part of the court."*

The Supreme Court, however, disagreed. In so doing, it placed considerable importance on the fact that the literal interpretation contended for by the Bank meant that the

*"... where a term of a contract is open to more than one interpretation it is generally appropriate to adopt the interpretation which is most consistent with business common sense."*

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<sup>1</sup> Court of Appeal: [2010] EWCA Civ 582; Supreme Court: [2011] UKSC 50

## Contract interpretation

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security was not available on the shipbuilder's insolvency, saying that it "*defies commercial common sense to think that this, among all other such obligations, was the only one which the parties intended should not be secured.*"

Consequently, whilst the Supreme Court reaffirmed that where the language in the contract is unambiguous, then the court must apply it. The Supreme Court went on to say that where there is ambiguity, generally the interpretation that is consistent with business common sense should be taken to be the interpretation intended by the parties.

The Supreme Court put it as follows:

*"The language used by the parties will often have more than one potential meaning. I would accept the submission made on behalf of the appellants that the exercise of construction is essentially one unitary exercise in which the court must consider the language used and ascertain what a reasonable person, that is a person who has all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract, would have understood the parties to have meant. In doing so, the court must have regard to all the relevant surrounding circumstances. If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other."*

And

*"where a term of a contract is open to more than one interpretation it is generally appropriate to adopt the interpretation which is most consistent with business common sense."*

This decision, arguably, reflects an emphasis on the perceived commercial realities that many Dispute Adjudication Boards and arbitrators have been quietly giving precedence to for many years. It does, however, place business common sense at the heart of contract interpretation when ambiguity arises, and so has important ramifications for all commercial contracts, not least construction contracts.

The language of complex construction contracts, including the layering of obligations through appendices, is often capable of more than one meaning. It remains the case that the aim of interpreting the relevant term is to determine what the parties meant by the language used, which involves ascertaining what a reasonable person with the background knowledge reasonably available to the parties at the time of the contract, would have understood the words used to mean.

But English law now calls for more weight to be given to "business/commercial common sense" and the commercial purpose of that which is being considered, and does not require a particular interpretation to give rise to an absurd or irrational result before having regard to that commercial purpose.

## Conclusions

Parties - and their advisors - must therefore give much more consideration to the possible commercial purpose and business common sense of a provision when disagreements arise and the provision is open to more than one interpretation. This means that they must also place less emphasis on a literal interpretation that might not sit with business common sense.

Further, in the drafting of commercial contracts, the parties - and their advisors - must now give greater thought to the inclusion of provisions that expressly confirm the commercial purpose of the agreement, and in particular the commercial purpose of any provision which might be said to be contrary to business common sense.

The facts in *Rainy Sky* provide a simple example: if it had been intended that the guarantees should not secure the insolvency of the shipbuilder, the recitals should have confirmed this to be the commercial intention of the parties, and included some explanation as to the reason for this unusual allocation of risk.

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## International arbitration: ICC Rules

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# Impact of the new ICC Rules on the management of construction arbitration cases

*In last year's Review, we discussed the new ICC Arbitration Rules which came into effect in January of this year. Frederic Gillion now reviews their impact. Most European international contractors will no doubt have noticed a significant increase in the number of arbitrations that they have had to commence or defend over the past 10 years. In fact, over that period, the workload of the Court of the International Chamber of Commerce (ICC) has grown by at least 40%, and between 2007 and 2010 the number of arbitration cases handled by the ICC has grown by 15%. Approximately 1,500 arbitration cases are currently being administered by the ICC. According to the latest statistics from the ICC (2010 Statistical Report), 17% of the 796 new cases filed in 2010 related to construction and engineering disputes, i.e. 135 new cases. Fifty per cent of the parties involved in the cases filed that year were from Europe.*

Is this trend symptomatic of a (new) belief that arbitration is an efficient way of resolving disputes for international construction projects? Probably not. This increase in the number of arbitration proceedings is most likely simply the result of an increase in the number of construction disputes, which in turn is a direct consequence of the severe financial difficulties experienced by both contractors and employers in recent years. Parties still rightly attempt to stay away from arbitration proceedings by seeking an amicable resolution of their disputes during the course of their projects. However, the current uncertain times sometimes make a settlement difficult to achieve, especially for public works projects where an additional layer of bureaucracy makes settlement discussions problematic.

It is still with a lot of reluctance (often to avoid limitation issues) that parties eventually start arbitration proceedings following the completion of a project, knowing that it will be a lengthy and costly process. Conscious of those concerns amongst users of international arbitration, the ICC has sought to promote in its new arbitration rules ("the 2012 ICC Rules") a more cost-effective, expeditious and efficient procedure for the resolution of disputes. The new procedural mechanisms and principles introduced by the 2012 ICC Rules are intended to improve case management, but what will the impact (if any) of these changes be on the conduct of construction arbitration proceedings?

*The arbitral tribunal and the parties have a new duty to "make every effort to conduct the arbitration in an expeditious and cost-effective manner, having regard to the complexity and value of the dispute."*

## Main concerns for parties involved in construction arbitrations: time and cost

Time and costs are beyond any doubt the two major concerns of parties involved in construction arbitrations. A recent survey conducted by the Chartered Institute of Arbitrators showed that the average costs for a UK claimant are £1.54m (£1,685,000 for claimants in the rest of Europe), with proceedings lasting on average between 17 and 20 months.

This survey was based on 254 arbitrations that took place between 1991 and 2010, of which a quarter related to construction/engineering disputes. Although the survey does not specify the average costs and time for construction arbitration proceedings, my experience is that any construction disputes of real significance commonly take anything between 2 and 4 years from the commencement of the arbitration to the final award, and that assumes that the arbitral tribunal has been diligent enough to render its final award fairly swiftly after the closing of the proceedings. A further year is also usually required to enforce that award.

In these difficult economic times, changes are undoubtedly needed to enable those disputes to be resolved in a much shorter time frame and in doing so to reduce the costs of the arbitration.

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## International arbitration: ICC Rules

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### Who is to blame for this situation?

In the spirit of openness, I should probably start with the parties' legal advisors who should accept some responsibility for the management of a case by assessing at an early stage the chance of success of some of their clients' claims so that no time is wasted arguing weak claims. Legal counsel should also identify from the outset the main issues of a case so that, if possible, a partial award may be made by the arbitral tribunal at an early stage of the proceedings. This can make a significant difference in the conduct of the case by increasing the pressure on one party and the chance of an early settlement as well as limiting the scope of the dispute. Finally, the parties' legal advisors should also ensure that any work given to experts is properly managed so that their scope of work is clearly defined.

Arbitrators are also partly to blame for the current situation. They can delay arbitrations in two ways: (1) their lack of availability for meetings and hearings, which is made worse in the case of a three-member arbitral tribunal; and (2) when drafting the award. A usual complaint with regard to arbitrators is that they take on too many cases at the same time (in the hope that some of them will settle early), making the management of each case a real challenge. I have been the unfortunate witness of a case where it took 18 months for the sole arbitrator to render his award. I have also been involved in some cases where it was clear that the arbitrators were not fully aware of the key issues of the case at the beginning of the proceedings, when it is often at this stage that they can assist the parties the most in fixing procedures that are swift and appropriate to the case.

Finally, arbitration institutions such as the ICC have a role to play in ensuring that the arbitration process is run in an efficient and cost-effective manner. This can be done through the clarification of the arbitration rules, but also by making sure that arbitrators, who genuinely have enough capacity to take on new cases, are appointed promptly. This is what the ICC has sought to achieve with its new rules of arbitration.

### The ICC's response to these concerns in the 2012 ICC Rules

The 2012 ICC Rules came into force on 1 January 2012 and will apply to all ICC arbitrations that commenced on or after that date, unless the parties have agreed that the previous version (1998) of the Rules will apply. The FIDIC forms of contract anticipate in their arbitration clause that all disputes shall be finally settled under the Rules of Arbitration of the ICC without specifying a particular version of the Rules. Construction disputes that arose under an unamended FIDIC contract will therefore be subject to the 2012 ICC Rules if the arbitration was commenced on or after 1 January 2012.

By and large, the 2012 ICC Rules maintain the main characteristics of ICC arbitration such as the terms of reference, the scrutiny of draft awards by the International Court of Arbitration (the ICC Court), and the involvement of national committees involved in the appointment of arbitrators. It is important to bear in mind that the ICC Court does not resolve disputes, but rather administers the resolution of disputes by arbitral tribunals and oversees the arbitration process. Many of the changes introduced by the 2012 ICC Rules in fact amount to a codification of current practice of the ICC Court and Secretariat. However, they also seek to address some of the concerns mentioned above by bringing in new procedural mechanisms and principles, including case management techniques focused on time and costs. I highlight below some of those changes that may improve the way ICC arbitration cases are managed. They include:

- New provisions regarding the appointment and availability of arbitrators;
  - Several updates and additions relating to the conduct of the proceedings to make them more efficient and cost-effective, including provisions on which arbitrators will be able to rely to sanction a party's delaying tactics when allocating costs between the parties; and
  - Indication of the timescale for the issuance of the award.
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*The new Rules have been carefully thought through and drafted, and appear fit for purpose.*

## International arbitration: ICC Rules

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### Appointment and availability of arbitrators

The ICC Court's power to speed up the appointment of arbitrators in order to address one of the traditional complaints made against the appointment of arbitrators by national committees (in particular the length of time it sometimes takes for those committees to appoint arbitrators and also the limited pool of arbitrators who are, as a result, very busy), the 2012 ICC Rules (Article 13) empowers the ICC Court to appoint arbitrators directly if it does not accept the proposal made by the national committee or no proposal is made within the time limit fixed by the ICC Court. The ICC Court may also appoint arbitrators directly in certain circumstances, including arbitrations involving a State entity.

### Requirement for arbitrators to sign a statement of availability

Article 11(2) of the 2012 ICC Rules requires any prospective arbitrator to sign before his appointment a statement confirming his availability for the case. In reality, this requirement simply confirms the ICC's practice to distribute to prospective arbitrators a form that requires them to disclose information not only about their independence, but also their availability to arbitrate a particular case. This new requirement in itself is therefore unlikely to avoid delays attributable to arbitrators.

The ICC is, however, conscious that this is a serious issue and both the ICC Court and its Secretariat will no doubt continue to place pressure on slow arbitrators when it comes to the drafting of awards, especially now that the 2012 ICC Rules have also introduced a requirement for arbitrators to inform the ICC Secretariat and the parties of the date when they anticipate their draft award being ready (see below).

## Conduct of the proceedings under the 2012 ICC Rules

### Mandatory case management conference

A case management conference must now form part of the arbitral process under Article 24 of the 2012 ICC Rules in order to consult the parties on the appropriate procedural measures at the outset of the proceedings. Article 24 further calls on the arbitral tribunal to hold subsequent case management conferences "to ensure continued effective case management", and under Article 24(4) the arbitral tribunal is specifically empowered to request the attendance of a party representative at a case management conference, the intention being to ensure the parties "buy in" to these procedural measures.

Appropriate procedural measures may include one or more of the case management techniques described in new Appendix IV which incorporates the ICC's publication Techniques for Controlling Time and Costs in Arbitration. None of these case management techniques are terribly new, but this Appendix IV does provide a useful reminder for the arbitral tribunal, and also for the parties and their legal advisors, of the procedural measures that can be used to control time and cost.

They include the following measures:

- (a) Bifurcating the proceedings or rendering one or more partial awards on key issues, when doing so may genuinely be expected to result in a more efficient resolution of the case. A usual bifurcation observed in construction cases is between issues of principle and quantum. Although this split is sometimes appropriate, it can however lead in some cases to a significant lengthening of the proceedings and therefore an increase of the overall costs;
  - (b) Identifying issues that can be resolved by agreement between the parties or their experts, typically issues of quantum in construction cases;
  - (c) Identifying issues to be decided solely on the basis of documents rather than through oral evidence or legal arguments at a hearing;
  - (d) Limiting disclosure of documents. This is particularly relevant to construction cases which tend to involve a considerable amount of documents;
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*In setting the arbitrators' fees, the ICC Court will take into account their "diligence and efficiency", "the time spent", the "rapidity of the proceedings", but also "the timeliness of the submission of the draft award."*

## International arbitration: ICC Rules

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- (e) Limiting the length and scope of written submission and evidence so as to avoid repetition and maintain a focus on key issues; and
- (f) Encouraging the parties to consider settlement.

### **New duty of the parties and arbitrators to conduct the arbitration in an expeditious and cost-effective manner**

Article 22(1) of the 2012 ICC Rules imposes on the arbitral tribunal and the parties a new duty to "make every effort to conduct the arbitration in an expeditious and cost-effective manner, having regard to the complexity and value of the dispute". The duty on the parties is confirmed by Article 37(5) which specifically authorises the arbitral tribunal to consider in its cost decision the extent to which each party complied with its general duty.

### **Timescale for the issuance of the award under the 2012 ICC Rules**

Finally, as mentioned above, the 2012 ICC Rules seek to address the issue of delays in the drafting of awards. At the close of the proceedings the arbitral tribunal must now inform the ICC Secretariat, as well as the parties, of the date by which the tribunal expects to submit its draft award to the Court for approval.

To reinforce that duty, a new Appendix III to the 2012 ICC Rules (on Costs and Fees) provides that in setting the arbitrators' fees, the ICC Court will take into account their "diligence and efficiency", "the time spent", the "rapidity of the proceedings", but also "the timeliness of the submission of the draft award". This may well work as an incentive for arbitrators to render their award within the anticipated timescale.

### **Conclusion**

Although not radical, the procedural mechanisms and principles introduced by the 2012 ICC Rules to improve case management may contribute to giving the parties more faith in the arbitration process by allowing them to have more certainty over the likely time and cost involved in pursuing a claim in arbitration. However, this will be so only if these mechanisms are implemented properly by the arbitrators and the parties, and also providing that the parties do buy in.

In principle, the parties should not have any difficulties in agreeing on a swift procedural timetable given that their common interest should be a speedy and efficient resolution of their dispute. However, the reality is that there will be cases where only one party may have interest in pushing for a resolution of the dispute (typically the claimant), while the other will do everything to delay the proceedings and the outcome of the case, and will ask for more time for more time to present its case. In that situation, the arbitral tribunal's main objective will be not to give priority to one argument over the other but rather to balance the parties' interests in the light of the particular dispute that it has to arbitrate.

Providing the opportunities given to the parties are equal, there should, however, be nothing stopping an arbitral tribunal from setting precise and narrow limits on matters such as the length of submissions or whether certain issues should be decided on the basis of documents only. In addition, tribunals can take advantage of the new rules relating to costs to sanction a party's wasteful tactics such as unmeritorious applications by making a partial award on costs against that party.

It is obviously too early to predict the impact of the 2012 ICC Rules on how arbitral tribunals will conduct arbitration proceedings. However, judging from the cases brought to ICC arbitration this year by clients of this firm, it would seem that arbitrators may well have embraced the ICC's new emphasis on case management and appear ready to stand up to the parties when determining the procedure of the arbitration by insisting in particular on shorter timetables.

*Legal counsel should also identify from the outset the main issues of a case so that, if possible, a partial award may be made by the arbitral tribunal at an early stage of the proceedings.*

## Dispute avoidance

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# Conflict avoidance and dispute resolution

*Nicholas Gould is the lead author of a Guidance Note recently published by the RICS entitled Conflict Avoidance and Dispute Resolution in Construction. Of course, many in the construction industry hope that they will never encounter a claim or a dispute. However, claims and disputes are simply symptoms of problems that have manifested themselves in relation to a project. It might be that a request for an extension of time or additional money for variations has not been dealt with, or that the contractor is simply losing money, or that defects have arisen during or after completion of the project.*

*As Nicholas explains below, attempts to deal with these issues (or rather avoid these issues arising altogether) require action at an early stage rather than simply waiting to see what happens and only responding when a dispute arises.*

Conflict avoidance requires clear, concise, careful and proper planning, of the strategy for the execution of a project. It is also about adopting a proactive conflict avoidance approach such as risk analysis, clarity in the contract documentation or partnering.

Dispute resolution on the other hand is about recognising when a dispute has arisen and appreciating the escalation of that dispute. Disputes can arise from ambiguity or the unclear definition of risk. An appreciation of the range of techniques that are available to resolve disputes is important, as is a need to recognise when expert or legal advice might be useful.

*Disputes can be reduced by checking that the contract documents are in place. This is not just about ensuring that the contracts are signed, it is also about ensuring that the correct documents are included within the document.*

## Conflict avoidance generally

There are a number of simple steps that can be taken in order to attempt to avoid conflict. These include:

- Good management: proactive planning and management of future work, as well as raising early issues of concern can avoid disputes;
- Clear contract documentation: Ambiguities in contract documents can lead to argument, disagreement and dispute. Focusing on the specific details of the particular project (rather than generalisation) is important;
- Partnering and alliancing: Building co-operation between the project participants and fostering team spirit is extremely valuable;
- Good project management: Planning ahead and managing generally and specifically the time, money and risks associated with the project is crucial;
- Good client management: Understanding the client's objectives and communicating issues and problems early on is fundamental;
- Good constructor management: A regular objective assessment of progress and the costs relating to a project also involves communicating well with the constructor and dealing positively and objectively with problems that arise. Do not ignore problems in the hope that they might go away;
- Good design team management: good information is crucial;
- Record keeping: Disputes can often be resolved by retrospectively considering records that have been kept during the project. However, those records are often not sufficiently detailed.

All these simple principles can help with any project. The more sophisticated the project, the more detailed a particular approach might need to be.

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## Dispute avoidance

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### Dispute resolution

There are three main techniques:

- Negotiation: The problem-solving efforts of the parties themselves;
- Mediation or conciliation: A third party intervening in order to assist the parties to resolve their difficulties;
- An adjudicative process: A final outcome is determined by a third party. This of course includes construction adjudication, but litigation and arbitration also lead to binding decisions based on an assessment of the facts and law.

These three core dispute resolution principles can be further sub-divided by particular techniques themselves. For example, expert determination is a contractual process where the parties agree that a third party will make a binding decision. The terms are governed by the contract. The decision of the expert will be final. It is, therefore, an adjudicative process.

The term ADR meaning alternative dispute resolution (although the term appropriate dispute resolution is far better) describes not just mediation. Any alternative to litigation (and arguably arbitration) that leads to a resolution of the dispute is alternative. So this could include rapid construction adjudication, the use of dispute boards and expert determination. Negotiation in itself is not really alternative as this is the widely used bedrock of all settlements. Mediation is alternative in that it helps the parties to reach that settlement more quickly, while expert determination is alternative in that a binding decision is imposed more quickly and more economically than by arbitration or litigation

### Contract documentation

A large number of standard form contracts are published and are widely available. This includes not just the JCT family, but also NEC3 as well as PPC, the old ICE contracts, the international FIDIC contracts and a range of other published forms, sub-contracts, collateral warranties, bonds and guarantees. Disputes can be reduced by checking that the contract documents are in place. This is not just about ensuring that the contracts are signed and dated, although that is extremely important and often overlooked in the construction industry. It is also about ensuring that the correct documents are included within the document. Consideration should be given to:

- The exact description of the contract (which edition, does sectional completion apply, and are there any supplements or amendments etc.);
- Inserting precise and correct details in the appendices, not just the completion date, but also the insurance provisions and other vital data; and
- Including in the contract the full text of any auxiliary documentation, such as guarantees, bonds, collateral warranties, etc.

A full copy of the contract should be kept for record purposes. It is not unusual for a key document to be misplaced during the course of a lengthy project. If a dispute arises in relation to an issue set out in that document, a lot of time and money can be spent trying to locate it.

### Multi-stage dispute resolution

The range of techniques that are available, and the commercial drive to find early and sensible resolution has led to the development of dispute escalation clauses. These are simply clauses that provide for several methods of resolving a dispute before finally ending up in litigation or arbitration. For example, the first step might be negotiation between senior executives of both parties. It is important to ensure that there is a clear timetable in respect of this procedure, otherwise it will be unenforceable. A court cannot force parties to settle their dispute, but they can enforce a timetable which requires parties to meet and discuss their differences.

*Claims and disputes are simply symptoms of problems that have manifested themselves in relation to a project.*

## Dispute avoidance

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Mediation could then be used as a second step, or occasionally as the first port of call.

More frequently a second step involves a binding decision by a third party. This will usually be a fast procedure such as expert determination. Adjudication under the Housing Grants, Construction and Regeneration Act 1996 (as amended by the Local Democracy and Economic Development and Construction Act 2009) must always be available "at any time" in respect of any construction contract covered by that legislation. Parties can therefore adjudicate at any time, but might save time and money by attempting a commercial negotiated or mediation based settlement procedure. Arbitration and litigation are of course always available as a final dispute resolution approach at this stage.

## Conclusion

Considering how disputes may arise and then taking proactive steps to avoid them is important for all of those involved in construction projects. Communicating well and looking for objective solutions and avoiding conflict can also help once the project is underway. A commercially based settlement, either in negotiation or by mediation is now frequently used in the construction industry. Use of a mediator or some other ADR process can resolve disputes more quickly, saving time and money. If all of this fails, there is of course the Rolls Royce procedures of arbitration or litigation. While they are applicable occasionally, they are best avoided if possible.

*Clear contract documentation: focusing on the specific details of the particular project (rather than generalisation) is important.*

## PS: Costs management pilot

You may recall from last year's Review, that Nicholas Gould is heading a team which is monitoring the effectiveness of the Costs Management Pilot, which started on 1 October 2011. The Pilot was scheduled to end on 30 September 2012 but has now been extended to March 2013. The purpose of the Pilot, as stated by Lord Justice Jackson in the introduction to the questionnaires being distributed by the courts to those participating in the Pilot, is to ascertain: (a) the benefits and disadvantages of costs management; and (b) how the process might be improved for the benefit of court users.

The Pilot will end just before the introduction in April 2013 of new rules on costs management. In line with the Pilot, parties will increasingly be expected to exchange costs budgets and will find that greater reliance is going to be placed on them. "Proportionality" has long been a phrase used by Judges when exercising case management powers, and there seems to be little doubt that this will include questions of cost management. In short, a costs management order will record the extent to which the budgets are agreed between the parties and, where not agreed, record the court's approval after making appropriate revisions. When a budget has been revised, the court will have to review, make any appropriate revisions and approve that budget.

Going back to the Pilot, an Interim Report was produced in February 2012. The findings should be considered to be preliminary, as the scheme had only been running for four months. However, with these caveats in mind, it seems that solicitors in general had a mixed opinion of the Pilot. Significant concerns were expressed that the Pilot actually resulted in increased costs due to the time taken to comply with it. Having said that, this aspect of the process should become easier to deal with once familiarity with it increases.

Importantly, respondents also highlighted that the Pilot was helpful in bringing early attention to costs and that this allowed their clients to better understand their potential liabilities (including their potential liability to the other party if they did not win). This is something which could also assist with settlement. This increased transparency in relation to costs, can only be of benefit to all parties. In relation to the judges, they generally seem to believe that the Pilot encouraged proportionality of costs to the value of the claim, that the current scheme worked well and so it did not require improvements. When the new rules come into effect, no doubt the courts will seek to control costs even further using their new case management powers.

## Mediation

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# Mediation: an update

*Mediation remains firmly at the forefront of the judicial radar. A new pilot mediation scheme has been set up in the Court of Appeal, in which its judges will normally refer appeals involving contractual, personal injury and clinical negligence claims with up to £100,000 at stake to mediation. Over the past 12 months, there have been a number of cases where the benefits of mediation have been rightly stressed. In *Faidi v Elliot Corporation*<sup>1</sup>, LJ Elias reminded the parties that “before embarking upon full-blooded adversarial litigation, parties should first explore the possibility of settlement.” However, as we set out below, the road to mediation is not always straightforward.*

## The enforceability of mediation agreements

In *Sulamerica CIA Nacional De Seguros SA & Others v Enesa Engenharia SA & Others*<sup>2</sup>, a dispute arose about two all risk insurance policies covering the construction of one of the world’s largest hydro electric facilities, in Brazil. Conditions 11 and 12 entitled “Mediation” and “Arbitration”, stated:

“11 ...If any dispute or difference of whatsoever nature arises...the parties undertake that, prior to a reference to arbitration, they will seek to have the Dispute resolved amicably by mediation...”

“12 ... In case the Insured and the Insurer(s) shall fail to agree as to the amount to be paid under this Policy through mediation ..., such dispute shall then be referred to arbitration under ARIAS Arbitration Rules.”

The question arose before Cooke J as to whether the right to arbitrate only arose if the requirements to mediate in condition 11 had been complied with. What had happened here was that the insurers had not sought to mediate prior to commencing arbitration. The insured argued that the mediation and arbitration clauses 11 and 12 were part of a single dispute resolution regime and that mediation was a condition precedent to arbitration under that regime. This meant that the commencement of arbitration proceedings was premature.

Here the Judge thought that there were a number of major difficulties which stood in the way of the submission that condition 11 was an enforceable obligation. First, there was no unequivocal commitment to engage in mediation. The Judge referred to and accepted the decision Mr Justice Ramsey in *Holloway v Chancery Mead*<sup>3</sup>, who expressed the view that an agreement to enter into a prescribed procedure for mediation is capable of giving rise to a binding obligation. However this was provided that matters essential to the process did not remain to be agreed.

However condition 11 did not meet those requirements, because it contained no unequivocal undertaking to enter into a mediation, no clear provisions for the appointment of a mediator and no clearly defined mediation process. The parties had agreed that “they will seek to have the Dispute resolved amicably by mediation” but did not bind themselves to do so in clear terms. The parties only agreed in general terms to attempt to resolve differences in mediation. There was no agreement to enter into any clear mediation process, whether based on a model put in place by an ADR organisation or otherwise. Finally, there was no provision for the selection of the mediator. This would all need to be agreed separately. Condition 11 by itself was not enough to establish what the parties had to do.

Therefore the court would not be able to determine whether or not a party had complied with the “obligations” allegedly imposed. If, for example, the parties were unable to reach agreement on a mediator or on the form of mediation and it was suggested that by one party that had not sought to have the dispute resolved by mediation, how would the court determine which party was in breach? Taken altogether, this meant that there was no condition precedent requiring the parties to mediate prior to any arbitration.

*“...before embarking upon full-blooded adversarial litigation, parties should first explore the possibility of settlement.”*

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<sup>1</sup> [2012] EWCA Civ 287

<sup>2</sup> [2012] EWHC 42 (Comm)

<sup>3</sup> [2007] EWHC 2495 (TCC)

## Mediation

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On appeal<sup>4</sup>, the Court of Appeal accepted that the parties intended the mediation clause to be enforceable and the court should be slow to hold that they had failed to achieve that objective. Nevertheless, each case must be considered on its own terms and, in this case, the clause was not effective in law because it failed to define the parties' rights and obligations with sufficient certainty. In particular, Lord Justice Moore-Bick noted that clause 11 did not set out any defined mediation process, nor did it refer to the procedure of a specific mediation provider. Finally, The Court of Appeal also rejected the insured's argument that, at the very least, the insurer was required to show that, as a matter of fact, it had satisfied condition 11. The court held that if "*mediation is not defined with sufficient certainty, the condition cannot constitute a legally effective precondition to arbitration.*"

### Failure to mediate (Part 1)

In the case of *PGF II SA v OMFS Co & Anr*<sup>5</sup>, on 10 January 2012, the day before the trial was due to start, PGF accepted a Part 36 offer that had been made on 11 April 2011. This left the question of costs. PGF at the time OMFS made their Part 36 Offer proposed mediation. No response was received. PGF tried again in July 2011. Again no response was received. PGF relied on the Halsey principle which says that, as an exception to the general rule that costs should follow the event, a successful party may be deprived of its costs if it unreasonably refuses to mediate. PGF said that the case was well suited to mediation. The Judge, Recorder Furst QC, noted that the skill of a mediator lies in drawing out seemingly intractable positions. The costs of mediation would not have been disproportionately high nor would it have caused delay.

OMFS said that it was not unreasonable for it to have refused to mediate given what had occurred between these parties at a previous mediation which had taken place in 2010 in relation to another dispute. The Judge was provided with letters which referred to the conduct of that mediation. OMFS further said that it had to wait until autumn 2011 before receiving full disclosure and the expert evidence on air conditioning, one of the main issues dividing the parties, was only exchanged in November 2011. Therefore it would not have been able to engage in a reasonable discussion as to settlement in April 2011.

The Judge held that it was unreasonable of OMFS not to respond to the suggested mediation. A party does not need to show that the mediation would have been successful, merely that it had a reasonable prospect of success. Here as in most cases, there was a reasonable prospect that well advised commercial parties, such as these, with the benefit of experienced lawyers would have been able to reach an accommodation. The Judge arrived at his decision without considering the conduct at the previous mediation. Mediations are covered by without prejudice privilege, which had not been waived by PGF.

Second, had PGF's conduct been a reason for refusing to participate in mediation in relation to this matter then one would have expected that to have been put forward by OMFS in answer to the invitation to mediate. Again the absence of expert valuation evidence on diminution in value was not raised at the time. Further PGF offered to provide OMFS with a copy of its report. The Judge noted that:

*"In general ... the court should be wary of arguments only raised in retrospect as why a party refused to mediate or as to why it cannot be demonstrated that a mediation would have had a reasonable prospect of success. First such assertions are easy to put forward and difficult to prove or disprove but in this case unsupported by evidence. Secondly, and in any event, it is clear that the courts wish to encourage mediation and whilst there may be legitimate difficulties in mediating or successfully mediating these can only be overcome if those difficulties are addressed at the time. It would seem to me consistent with the policy which encourages mediation by depriving a successful party of its costs in appropriate circumstances that it should also deprive such a party of costs where there are real obstacles to mediation which might reasonably be overcome but are not addressed because that party does not raise them at the time. I have little doubt that that is the position here, namely that any such inhibitions to mediation could have been overcome at the time..."*

*"The Defendant's attitude in simply refusing even to contemplate the possibility of mediation on the grounds that the claim was utterly hopeless was an unreasonable position to take."*

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<sup>4</sup> [2012] EWCA Civ 638

<sup>5</sup> [2012] EWHC 83 (TCC)



## Mediation

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### Failure to mediate (Part 2)

In *Mason and others v Mills & Reeve (A Firm)*<sup>6</sup>, one of the issues that the Court of Appeal had to consider was an appeal by the successful party against the decision to impose a costs penalty for having refused to participate in a mediation. This refusal was despite the fact that proposals for ADR had not just been made by the claimants but also the trial judge. The position of the defendant was that the claim had no merit, a view that had been vindicated at the trial. The view, however, of the trial judge was that claimants' prospects of success "was at variance with the result in the judgment in a number of respects." He in particular noted that a successful mediation would have avoided the risk of "collateral reputational damage" to the defendant and also that mediation would have allowed both parties to gain a better understanding of the weaknesses of their cases something which might have encouraged a settlement. This led the trial judge to hold that:

*"It seems to me that the Defendant's attitude in simply refusing even to contemplate the possibility of mediation on the grounds that the claim was utterly hopeless was an unreasonable position to take. Accordingly, I consider that the Defendant's attitude to mediation is a factor that should be brought into account in making an overall assessment of what costs order should be made."*

The Court of Appeal did not agree with this approach. Davis LJ stressed that the trial Judge had found that the defendant had been "vindicated" in its assessment of the strength of the claimants' case which meant that its position, maintained throughout, had been shown to be justified. Further the Judge did not explain what "weaknesses" in the respective cases would have been revealed in a mediation. It was also not said that if identified, their revelation could have led to a mediated settlement. In addition Davis LJ did not understand why avoidance of "collateral reputational damage" to the defendant should have been considered a relevant factor, counting against the defendant. A settled professional negligence claim was capable, in some instances, of leaving behind reputational damage. Some professional defendants might, entirely reasonably, wish publicly to vindicate themselves at trial in respect of claims which will have been publicly aired by the commencement of proceedings. The Judge noted:

*"It would be unfortunate if claimants in cases of this kind could be encouraged to think that such a consideration as identified by the judge could enhance their bargaining position."*

Davis LJ also had concerns in respect of the trial Judge's assessment that the possibility of a mediated settlement was "not unrealistic". At all stages the parties "in reality were a hundred miles apart." The claimants had sought £750k and costs. The defendant's best offer had never been more than a "drop hands" approach. It was therefore difficult to see how a mediation could have had reasonable prospects of success. Further, unlike many cases, nothing changed to necessitate a re-evaluation on the question of liability. Davis LJ concluded that:

*"A reasonable refusal to mediate does not become unreasonable simply by being steadfastly, and for cause, maintained."*

The key historic decision in these types of cases is, of course, the *Halsey*<sup>7</sup> case. Davis LJ noted that the Court of Appeal here was concerned to make clear that parties were not to be compelled to mediate, saying that ADR was not appropriate for every case. The Court of Appeal in *Halsey* also identified the situation where a party reasonably believes that he has a strong case as being the type of situation where ADR might not be appropriate, otherwise there was scope for a claimant to use the threat of costs sanctions to extract a settlement even where the claim is without merit. This was the situation here. The unsuccessful party (the claimants) was not therefore able to show that the successful party (the defendant) had acted unreasonably in refusing to agree to mediate. This led the Court of Appeal to reassess the original costs order, that the claimants pay 50% of the defendant's costs. This reassessment could only be done with what was described as a broad brush which led the Court of Appeal to increase the percentage of costs awarded to the defendant to 60%.

*"...the court should be wary of arguments only raised in retrospect as why a party refused to mediate or as to why it cannot be demonstrated that a mediation would have had a reasonable prospect of success."*

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<sup>6</sup> [2012] EWCA Civ 498

<sup>7</sup> *Halsey v Milton Keynes NHS Trust* [2004] EWCA Civ 576

## Building Information Modelling (BIM)

# Building Information Modelling (BIM) & English law

*The key to the successful implementation of BIM is not in the legal nuances – its success depends on close collaboration at the outset with the client, contractors, consultants and suppliers.*

*The government’s construction strategy requires that all government projects utilise a fully collaborative 3D computer model (Level 2) by 2016, with all project and asset information, documentation and data being electronic. There is no doubt that BIM is the construction industry’s buzzword at the moment, but as Stacy Sinclair considers, what are the legal and contractual implications of the implementation of BIM on your project?*

BIM, as defined by the Construction Project Information Committee and supported by the RIBA, is the:

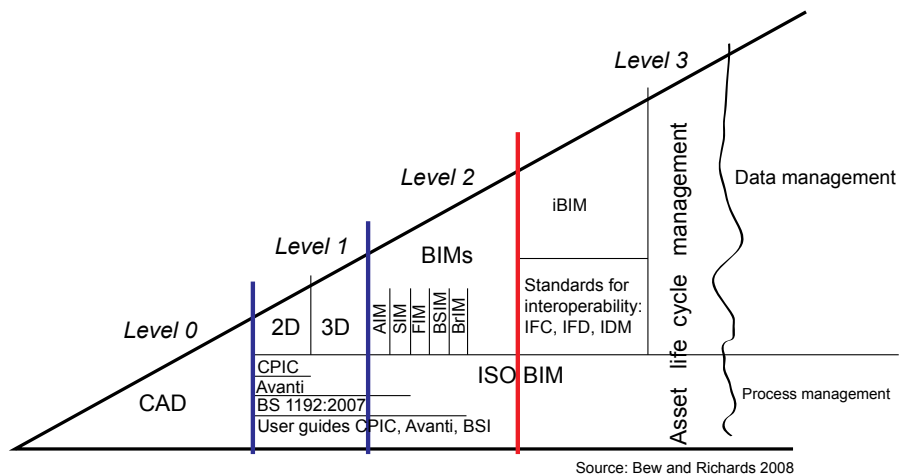
*“digital representation of physical and functional characteristics of a facility creating a shared knowledge resource for information about it forming a reliable basis for decisions during its life cycle, from earliest conception to demolition”.*

In other words, BIM is a way of approaching the design and documentation of a project, utilising 3D computer technology which is shared amongst the design and construction teams, incorporating cost, programme, design, physical performance and other information regarding the entire lifecycle of the building in the construction information/building model. BIM is not simply the use of 3D technology – it is a way of design and construction.

As the use of BIM spreads throughout the construction industry, concerns regarding its legal and contractual implications rise. In particular:

- Does the use of BIM alter the traditional allocation of responsibilities as between the client, contractors, designers and suppliers?
- How (if at all) should standard form appointments and building contracts be altered to account for the use of BIM?
- Does the party managing the model assume additional liabilities and risk?

Before considering the answers to these questions, it is imperative that both the parties and their advisors understand what BIM environment they are working in. In 2008, Mark Bew of BuildingSmart and Mervyn Richards of CPIC developed the BIM Maturity Diagram a now well-known diagram, set out below, which acknowledges the impact of both data and process management on BIM and defines various levels of maturity for BIM.



## Building Information Modelling (BIM)

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In short, Level 2 BIM provides data and information in a 3D environment, with each member of the design (& possibly construction) team creating and maintaining their own model. These models and databases then “fit” or work together with the use of proprietary technology (this consolidated model, comprised of the individual models prepared by each disciple, is often referred to as a “federated model in a Common Data Environment (CDE)”). On the other hand, Level 3 BIM utilises a single project model, accessible by all team members.

### Any change in the traditional legal position?

The consensus now appears to be that the use of BIM at Level 2 does not require whole sale changes to the traditional forms of contract or the allocation of responsibilities as between the parties. However, as BIM moves towards Level 3 in the future, changes to building contracts may well be required as the traditional legal position and relationships between the parties are likely to change.

In March 2011, the Government Construction Client Group (GCCG) concluded in its Strategy Paper that:

*“...little change is required in the fundamental building blocks of copyright law, contracts or insurance to facilitate working at Level 2 of BIM maturity. Some essential investment is required in simple, standard protocols and services schedules to define BIM-specific roles, ways of working and desired outputs. Looking forward to the achievement of Level 3 integrated working, there are limited actions related to contracts, appointments and insurance that could be taken in advance to facilitate early adoption of integrated working.”*

With the government’s current focus on Level 2 BIM, establishing a BIM Protocol and its associated services schedules on each project is clearly of utmost importance in structuring the project’s design and development processes as well as addressing any legal concerns.

### The BIM Protocol

At present, there is not a UK standard BIM Protocol as such – though they are likely to be available in the near future. Appendix 20 of the GCCG’s Strategy Paper did provide an illustrative draft of a BIM Protocol for discussion; however, this protocol is likely to be considered too brief. By way of example, it does not fully address intellectual property issues.

The US on the other hand has developed several standard BIM Protocols and execution plans: the AIA E202, ConsensusDOCS 301 BIM Addendum and the Penn State BIM Execution Guide. These documents are not intended to restructure contractual relationships or stand as a substitute for a complete building contract. They are simply addendums to be appended to the building contract and consultant appointments.

These documents address important design, data and process issues which must be determined at the outset of a project: intellectual property rights, level of development (level of definition) of the model, model management, allocation of risk, ownership, permissible uses of the model, schedule of BIM deliverables, etc.

Whether or not the BIM Protocol is a contractual document and to what extent can the contractor and design professionals rely on each others models are important issues to confront and address in the BIM Protocol.

To have any legal recourse, parties are likely to require that the BIM Protocol is indeed a contractual document. Most recently, the JCT contract amendments, introduced in December 2011 in the Public Sector Supplement (Fair Payment, Transparency and Building Information Modelling), require any BIM Protocol to be a Contract Document. The Public Sector Supplement amends the definition of Contract Documents to be found at clause 1.1 of many of the JCT standard forms to include:

*“any agreed Building Information Modelling protocol”.*

***“Looking forward to the achievement of Level 3 integrated working, there are limited actions related to contracts, appointments and insurance that could be taken in advance to facilitate early adoption of integrated working.”***

## Building Information Modelling (BIM)

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As regards to the level of reliance on the parties' models (Level 2 BIM), the ConsensusDOCS 301 BIM Addendum allows parties to choose whether:

- each party represents that the dimensions in their model are accurate and take precedence over the dimensions called out in the drawings; or
- each party represents that the dimensions in their model are accurate to the extent that the BIM Execution Plan specifies dimensions to be accurate, and all other dimensions must be retrieved from the drawings; or
- the parties make no representations with respect to the dimensional accuracy of their models and they are to be used for reference only - all dimensions must therefore be retrieved from the drawings.

In order to avoid complicated and potentially expensive disputes in the future, any BIM Protocol should address this dimensional accuracy/level of reliance issue along with the scope of the models created (often referred to as Level of Definition).

### The Information Manager

Finally, a further legal issue which must be considered at the outset is the role, responsibilities and liabilities of the Information Manager – a key member of the design and construction team required for the successful implementation of BIM. A fundamental question which is likely to arise is this: if each party is responsible for their own model, to what extent is the Information Manager liable when clashes are not detected or the design is not coordinated?

The draft PAS 1192-2:2012 requires the Information Manager to:

*"provide a focal point for all information modelling issues in the project; ensure that the constituent parts of the Project Information Model is compliant with the MIDP [Master Information Delivery Plan]; [and] ensuring that the constituent parts of the Project Information Model have been approved and authorized as "suitable for purpose" before sharing and before issuing for approval".*

The specification goes on to state that the Lead Designer shall be responsible for the coordinated delivery of all design information. As such, the role of the Information Manager is not meant to be that of the Lead Designer – the Information Manager is responsible for the management of information, information processes and compliance with agreed procedures, not the coordination of design.

If the parties agree that this is the role of the Information Manager, clearly this needs to be identified and dealt with in the BIM Protocol - otherwise a potential conflict arises as regards to design and design coordination roles.

### Conclusions

The key to the successful implementation of BIM is not in the legal nuances – its success depends on close collaboration at the outset with the client, contractors, consultants and suppliers and the establishment of a well developed BIM Protocol.

Level 2 BIM is unlikely to change the current legal landscape of the construction industry, provided the BIM Protocol addresses risk allocation and other elements touched on above. As we see a move towards Level 3 BIM, contractual relationships and risk are likely to change – therefore resulting in more sophisticated contractual arrangements.

***"Companies who fail to adopt BIM run the risk of being "Betamax'd out" in years to come."***<sup>1</sup>

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<sup>1</sup> The comments of Paul Morrell, the government's chief construction advisor at NBS round table event in May 2011.

## EU Procurement

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# EU Procurement: abnormally low and non-compliant tenders

*In the current economic climate, with budgets significantly reduced, councils and other contracting authorities are coming under more and more pressure to reduce costs. Procurement and competitive tendering is an obvious route to making economic savings. However in times of recession, tenderers can sometimes be moved to put in a bid that might be considered to be low, even abnormally low. What protection is there for other tenderers and what should a contracting authority do in these circumstances?*<sup>1</sup>

For the contracting authority, there are, of course, two considerations: first, what if the bid is so low that ultimately it could lead to higher costs and/or performance issues over the duration of the contract; and second what is the position of the other parties to the tender process? Can they challenge the tender process if the contract is awarded to a tenderer who is thought to have submitted an abnormally low price?

Contracting authorities can award a contract on the basis of either the lowest price (which is not permitted for competitive dialogue and is not suitable for negotiated procedure) or the most economically advantageous offer (taking into account criteria linked to the subject matter of the contract, such as price, quality, technical merit, cost-effectiveness, delivery date and aesthetic and functional characteristics). The Regulations do not define what constitutes an "abnormally low" offer, nor is there much helpful guidance to date on the point from the ECJ or the courts. Possible things to look out for include:

- (i) Significant variations from the other bids;
- (ii) A bid that comes in, in whole or in part, below what the contracting authority was expecting based on its own market knowledge and costings;
- (iii) The assumption of greater risk than had been anticipated.

The risks to the contracting authority include:

- (i) Non-performance;
- (ii) Missing out on a better overall tender package;
- (iii) Greater overall costs; including additional management costs and post tender variations;
- (iv) The costs of retendering; and
- (v) Legal costs of a procurement challenge

Under Regulation 30(6), if an offer for a public contract is abnormally low, the contracting authority can reject it, but only after it has: requested in writing from the bidder an explanation of the offer or part of the offer which it considers to be abnormally low, taken account of the evidence provided in response to the request and subsequently verified the offer or parts of the offer being abnormally low with the bidder (Reg 30(6)(c)). Regulation 30(7) sets out the types of information that may be requested under Reg 30(6). This could include: the economics of the method of construction, manufacturing process or services provided; any technical solutions suggested by the bidder, or exceptionally favourable conditions available to the bidder; the originality of the works, goods or services to be provided; compliance with relevant local employment/working conditions and the possibility of the bidder obtaining state aid.

In *Varney v Hertfordshire County Council*<sup>2</sup> Varney was one of the unsuccessful tenderers for the contracts for the operation of the 18 Household Waste Recycling Centres. Flaux J held that a contracting authority cannot reject an offer that is abnormally low unless it has investigated certain aspects of that offer. In other words, the relevant provisions

*An abnormally low tender which may be rejected is one that is priced at such a level that the authority considers itself, in all the circumstances, unable to rely upon the contract being properly performed.*

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<sup>1</sup> Unfortunately, the limited legal protection which we review here only applies to tenders in the public and not the private sectors.

<sup>2</sup> [2010] EWHC 1404

## EU Procurement

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operated purely so as to provide procedural protection for a tenderer whose bid might be rejected as being abnormally low, and created no duty in favour of other tenderers. Varney, had argued that the council was under a general duty to investigate tenders that are abnormally low generally. Flaux J rejected this, stating that there was nothing in the Directive or the Regulations to support such a contention. Such a duty could only arise where the council either knows or suspects that the tender in question is abnormally low. The Regulations only require a contracting authority to investigate a tender that appears to it to be abnormally low and which it proposes to reject for that reason.

### So what can the contracting authority do?

Certainly, the prudent contracting authority, where it has concerns that any bid is abnormally low, should fully investigate whether that bid is sustainable. But that is a matter of commercial common sense as much as it is one of good procurement law practice. An abnormally low tender which may be rejected is one that is priced at such a level that the authority considers itself, in all the circumstances, unable to rely upon the contract being properly performed. That conclusion might follow even if the contract was not actually loss-making, if it did not generate a normal level of profit, but it would not necessarily follow if losses would be sustained.

In the UK, there is of course no domestic legislative definition to draw upon. In theory, the issue of whether a particular tendered price is abnormally low might be viewed from two perspectives: comparison with some absolute standard; or comparison with the other bids received. The most obvious absolute standard would be the normal market price, but save in the case of fairly straightforward contracts there may often not be an established market price against which comparisons may readily be made. Another possible standard might be the authority's own pre-estimate of what it expects to have to pay for the service in question, but the authority may be ill-equipped to make an accurate estimate, especially in a fluid and changing market, or in the case of a complex or unusual contract.

In *Varney*, there was another bid which was a suspected abnormally low bid. The other tenders were not considered abnormally low, because they were consistent with one another and did not deviate from the mean average of all tenders received for the sites for which they had tendered. This is the "anomaly threshold" test. An authority has a discretion as to what test it uses for identifying what may be an abnormally low tender and it is permissible to use a comparison with the average of the tenders submitted for the contract as a threshold for determining whether a tender is abnormally low.

The Council had also investigated the tender price against the likely cost of performing the relevant services. To take site attendance costs, they were expecting to pay more by way of site attendance charges under the new contracts. The abnormally low contract stood out because its proposed site attendance charges were all less than was being charged under the existing contract. Finally, what happened in the *Varney* case was that three of the sites were awarded to the tenderer who had the abnormally low overall tender. Whilst it was felt too much of a risk to offer more than the three sites, the Council felt that it was a risk worth taking to offer them the sites they already operated. The court agreed. The evidence showed that there was no evidence that the tenders for the three sites had been unsustainable and that overall the contracts were making a small profit.

### When may a tender be rejected as abnormally low?

Having called for and received an explanation of the pricing, what conclusion has to be reached based on that explanation before the right to reject the bid arises? Where there is no pre-defined method of identifying tenders that appear abnormally low and may call for an explanation, the answer to this question will also serve to define what an authority should be looking out for when tenders are received. Fundamental though this question is, there appears to be no authority that addresses it directly.

Various formulae appear in the decisions of the European Court. They include whether the bid is "genuine" (Lombardini)<sup>3</sup> and whether it is "reliable and serious" (T-4/01 Renco SpA<sup>4</sup>). These formulae are not entirely helpful. What is meant by asking whether a bid is "genuine"

*The existence of a proper exchange of views to enable the tenderer to demonstrate that its tender is genuine constitutes a fundamental requirement in order to prevent the contracting authority from acting in an arbitrary manner and to ensure healthy competition.*

<sup>3</sup> *Impresa Lombardini* [2001] EUJ C-286/99

<sup>4</sup> *Renco SpA v Council of the European Union* [2003] E.C.R. II-17

## EU Procurement

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or “serious”? It would be right to assume that the bidder wants to win the bid - otherwise he would bid artificially high, not low. Does the bidder truly intend to fulfil the contract at the tendered price, or will he increase the price by charging for various “extras”, or by threatening to walk off the contract? Remember that it will normally be difficult to mount a successful challenge to the authority’s decision to accept the bid, unless the issue has been ignored altogether.

Some judicial guidance on abnormally low tenders came in March 2012, when the European Court heard a preliminary reference from a Slovak court on the extent of obligations on authorities to seek clarification in relation to (a) abnormally low tenders, and (b) non-compliant tenders.

### Case C-599/10 SAG ELV Slovensko and Others

This case involved the award of a contract for the supply of toll collection services on motorways and roads in Slovakia. Tendered using the restricted procedure, clarifications had been sent to two (ultimately unsuccessful) bidders in relation to a number of aspects of their tenders including in relation to what were said to be abnormally low prices. Both replied, but they were then excluded from the tender process. Both bidders appealed and the Slovak Supreme Court asked the CJEU for a preliminary ruling on whether a contracting authority was obliged to seek clarifications from bidders where an abnormally low tender is suspected before excluding that tender?

The answer to that question was yes. The CJEU considered previous EU case-law on the rules governing abnormally low tenders, and in particular the *Lombardini* case. Article 55 makes it mandatory for a contracting authority to examine the details of tenders that are abnormally low in order to prevent the contracting authority from acting in an arbitrary manner and to ensure healthy competition between undertakings:

*“Accordingly, the existence of a proper exchange of views, at an appropriate time in the procedure for examining tenders, between the contracting authority and the tenderer, to enable the latter to demonstrate that its tender is genuine, constitutes a fundamental requirement of Directive 2004/18, in order to prevent the contracting authority from acting in an arbitrary manner and to ensure healthy competition between undertakings.”*

### Non-compliant tenders

The judgment is, however, more helpful on the general question as to the extent of obligations on authorities to seek clarification before deciding to reject a tender for being imprecise or non-compliant or failing to meet the tender specifications. In contrast to the situation concerning abnormally low prices, there are provisions which expressly set out the procedure to be followed in the event that the contracting authority finds, in a restricted public procurement procedure, that the tender submitted by a tenderer is imprecise or does not meet the technical requirements of the tender specifications.

Remember that, in principle, once tenders have been submitted, those tenders can no longer be amended either at the request of the authority or at the request of the tenderers. The principle of equal treatment of tenderers and the obligation of transparency preclude, in that procedure, any negotiation between the contracting authority and one or other of the tenderers. To enable the contracting authority to require a tenderer whose tender it regards as imprecise or as failing to meet the technical requirements of the tender specifications to provide clarification in that regard would be to run the risk of making the contracting authority appear to have negotiated with the tenderer on a confidential basis, in the event that that tenderer was finally successful, to the detriment of the other tenderers and in breach of the principle of equal treatment.

Therefore, an authority will not be obliged to seek clarification of a tender when it will be rejected because it fails to meet the technical requirements. However, an authority can, exceptionally, seek the correction or amplification of a tender, particularly where mere clarification is required, or to correct obvious material errors, provided that such amendments do not amount to a new tender. Such a request can be made only after the

*The Court will only extend the 30-day time limit, if there is a good reason to do so: “a good reason will usually be something which was beyond the control of the given Claimant; it could include significant illness or detention of relevant members of the tendering team.”*

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authority has looked at all the tenders. Further, the request must be sent to all tenderers in the same situation, unless there are objective grounds to justify different treatment for example if the tender must be rejected in any event. If an authority chooses to seek clarification, it must do so in respect of all elements that are imprecise and it cannot then reject the tender on the basis of an element on which it did not seek clarification.

### A UK approach - can you prohibit caveats in tenders?

*In Turning Point Ltd v Norfolk County Council*<sup>5</sup>, Mr Justice Akenhead considered issues of limitation as well as qualifications/caveats to tenders in public procurement. In December 2011 the Council invited Turning Point and others to tender, sending them the ITT which included a condition that the Council “will accept no caveats to proposals or variant bids...”

***The Judge did not consider that the Council should have sought clarifications before rejecting their tender as the ITT had made it clear there were to be no qualifications or caveats – a requirement which was “perfectly fair, reasonable and common.”***

Turning Point raised a number of questions on the ITT. The Council responded in January 2012. Despite this, Turning Point still considered that the information provided was inadequate or incomplete. Nevertheless, Turning Point submitted a tender, which included a Note on their pricing schedule which amounted to a clear caveat.

On 12 March 2012, the Council informed Turning Point that they had not been successful as their tender contained a qualification. Turning Point complained and on 28 March 2012 issued proceedings claiming that the information provided at the tendering stage was wholly inadequate and incomplete. The Council asserted that the proceedings were brought too late as they were not within 30 days of when Turning Point either did or should have become aware of the inadequacies (if any) in the tender information - as required by Regulation 47D. Mr Justice Akenhead agreed that the allegations were time-barred. He considered that Turning Point must have known of the inadequacies (if any) of the information by no later than 9 February 2012 when they submitted their tender to the Council. Turning Point had not issued their claim until 28 March 2012. Whilst the court may extend the 30-day time limit, the Judge did not consider that there was any good reason to do so. He stated that:

*“a good reason will usually be something which was beyond the control of the given Claimant; it could include significant illness or detention of relevant members of the tendering team.”*

With regard to the Note, Mr Justice Akenhead held that this was a clear qualification or at the very least a caveat. Had the Council accepted it, they would have been responsible for redundancy costs. The Judge did not consider that the Council should have sought clarification from Turning Point before rejecting their tender as the ITT had made it clear that there were to be no qualifications or caveats - a requirement which he considered was perfectly fair, reasonable and common. Furthermore, there was no express entitlement within the ITT for the Council to go back to tenderers on the pricing schedule for clarification - nor did he consider there to be an implied obligation for the Council to do so.

### If seeking clarification, remember to ask everyone

The principles in the Slovak case were followed in *Clinton v Department for Employment and Learning*<sup>6</sup> where the ability to seek the clarification of tenders was considered by the High Court in Northern Ireland. Here, 13 tenderers were invited by the authority to clarify their tenders, but not Clinton. Clinton was later excluded as it had failed to provide sufficient evidence of its experience. It argued that by asking other tenderers to supplement areas of their tenders, but not Clinton, the authority had breached its duty of equal treatment.

The High Court agreed. The authority had a discretionary power in the ITT to seek clarification from tenderers. Failing to use that discretion to clarify the claimant’s tender, when it had specifically sought clarification of tenders submitted by others in a similar (if not the same) position, infringed the duty of equal treatment. Seeking clarification from Clinton would have complied with the principles of legal certainty and good administration. This meant that the original tender decision was set aside.

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<sup>5</sup> [2012] EWHC 2121 (TCC)

<sup>6</sup> [2012] N1QB2



## International arbitration

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# International arbitration: choice of law and bilateral investment treaties

*We have previously mentioned the Sulamerica CIA Nacional De Seguros SA and others v Enesa Engenharia SA and others case (see page 13). As well as providing some useful comments on the enforceability of mediation agreements, the Court of Appeal decision provided helpful guidance on determining the proper law of an arbitration agreement where there is no express choice of law and in relation to drafting mediation and dispute resolution clauses.*

The case was an appeal against the order of Cooke J continuing an anti-suit injunction restraining the appellants, Enesa, from pursuing proceedings against the respondents, Sulamerica, in the Brazilian courts. The insured, Enesa, entered into two all-risk insurance policies with the insurer, Sulamerica, in connection with the construction of a hydroelectric generating plant in Brazil. The policies contained a London arbitration clause, an express choice of Brazilian law as the law governing the contract and an exclusive jurisdiction clause in favour of the Brazilian courts.

On 29 November 2011, Sulamerica gave Enesa notice of arbitration. In response Enesa commenced proceedings in Brazil in order to establish that Sulamerica was not entitled to refer the dispute to arbitration and obtained an injunction from the court in Sao Paulo restraining the insurer from resorting to arbitration in order to pursue a claim for a declaration that they were not liable under the policy. Subsequently, Sulamerica made an application to the Commercial Court successfully seeking an injunction restraining Enesa from pursuing the proceedings in Brazil.

The issue before the Court of Appeal therefore concerned the choice of proper law of the arbitration contract. Leaving aside the requirement for mediation prior to arbitration, the policy contained an express choice of Brazilian law as the governing law of the agreement, together with an exclusive jurisdiction clause referring disputes to the Brazilian courts. However, the arbitration was to be seated in London if the parties did not agree on the amount to be paid under the policy.

Following a review of authorities on the subject (which the Court of Appeal commented were not entirely consistent), LJ Moore-Bick established that two propositions provided the starting point for any enquiry into the proper law of an arbitration agreement.

First, even if the agreement formed part of a substantive contract (as is commonly the case), its proper law might not be the same as that of the substantive contract. Secondly, the proper law should be determined by undertaking a three-stage enquiry into (i) express choice, (ii) implied choice, and (iii) closest and most real connection. As a matter of principle, those three stages ought to be embarked on separately and in that order, since any choice made by the parties ought to be respected, but in practice stage (ii) often merged into stage (iii), because identification of the system of law with which the agreement had its closest and most real connection was likely to be an important factor in deciding whether the parties had made an implied choice of proper law.

Deciding that the implied choice was English law, LJ Moore-Bick looked at the intentions of the parties and the specific factual circumstances surrounding the case, and took account of the fact that it was Enesa's case that under Brazilian law, the arbitration agreement would only be enforceable with its consent. If correct, this would significantly undermine the arbitration agreement. Furthermore, there was nothing to indicate that the parties intended to enter into a one-sided arrangement of that kind. The possible existence of a rule of Brazilian law that would undermine the referral to arbitration of disputes suggested that the parties did not intend the arbitration agreement to be governed by that law. The choice of London as the seat assumed acceptance that the arbitration agreement would be conducted under the Arbitration Act 1996. Therefore, the supervisory jurisdiction was held to have a closer connection to the arbitration agreement in this case than the law of the insurance policy whose purpose was unrelated to that of dispute resolution.

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*If the chosen seat of arbitration is in England, it is important to state expressly which law shall govern the agreement to arbitrate, even if the agreement to arbitrate is incorporated into the main agreement as a clause forming part of the main agreement which already contains a jurisdiction clause.*

*The UNCITRAL tribunal agreed with White Industries that the nine-year delay by the Indian courts in acting to enforce White Industries' award amounted to a breach of India's obligation to provide an effective means of enforcing its rights.*

## International arbitration

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### Conclusion: drafting arbitration agreements

What this means is that to avoid uncertainty, if the chosen seat of arbitration is in England, it is important to state expressly which law shall govern the agreement to arbitrate, even if the agreement to arbitrate is incorporated into the main agreement as a clause forming part of the main agreement, and that main agreement already contains a jurisdiction clause.

### Bilateral investment treaties

Bilateral investment treaties (BITs) are agreements between two States which are intended to promote trade between those two countries. All BITs are different. However, they typically contain clauses protecting the rights of investors from one State when making investments in the other.

The types of rights which are typically protected include:

- the right to receive equal treatment to that given to local companies and to other foreign investors
- the right not to have your investment taken (or expropriated) by the Government; and
- the right to insist that the Government honours its obligations under a contract.

BITs will usually allow an aggrieved investor to bring an action directly against the host State Government in international arbitration, rather than having to bring any action in the host State's own courts.

BITs can be directly relevant to companies working in the construction and engineering sectors as investment treaty cases have found that construction contracts are an investment which can be protected. Therefore, if the actions of a host State (whether in its capacity as a project participant or in another regulatory or enforcement capacity) causes an 'investor' to suffer losses in connection with a project, a remedy may be available under a BIT (if one exists between the host State and the investor's home State).

If you do have a claim under a Bilateral Investment Treaty, that claim is made not against your contract counterparty directly (unless that counterparty is the government) but against the central government, for failing to ensure that one of its subdivisions or agencies complied with their treaty obligations.

Claiming directly against a host State could obviously have serious commercial (and political) implications. However, this is becoming an increasingly popular method of protecting investor rights in foreign countries and the final awards are more easily enforced than private international arbitration awards. When you are looking at business opportunities in a new country – or if you have a large value dispute which has proven difficult to resolve – it is worth investigating whether a BIT remedy may be available.

### The India decision – *White Industries Australia Ltd v Republic of India* (UNCITRAL)<sup>1</sup>

Coal India Limited (CIL) and White Industries Australia Limited signed an agreement in September 1989 for the turnkey development of the open-cast coal mine at Piparwar in Uttar Pradesh, India. The agreement contained an arbitration clause providing for ICC arbitration with Paris as the seat.

During the course of the project, disputes arose in relation to the deduction of penalties by CIL. Ultimately these were referred to arbitration. In March 2002 an ICC Tribunal issued a substantial award in White Industries' favour. From 2002 onwards White Industries attempted, unsuccessfully, to enforce that award through the Indian courts. At the beginning of 2012, the action had reached the Supreme Court.

<sup>1</sup> The UNCITRAL arbitral decision was dated 30 November 2011

## International arbitration

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In July 2010, frustrated with the lack of progress, White Industries commenced an action against India under the Australia-India BIT, claiming that India had breached its treaty obligation to provide a foreign investor with “effective means of asserting claims and enforcing rights”. What was interesting here was that this obligation was not one which was within the Australia - India BIT itself, but in a BIT entered into between India and Kuwait.

However, the Australia - India BIT did contain what is known as a “most favoured nation” clause which means that White Industries were also to make use of provisions in other BITs if the provisions of that other BIT gave investors of another nation greater protection. White Industries also claimed it had been denied justice in violation of the obligation to provide “fair and equitable treatment” to foreign investors.

Having decided that the ICC award was “an investment” which could be protected under the BIT, the UNCITRAL tribunal agreed with White Industries that the nine-year delay by the Indian courts in acting to enforce White Industries’ award amounted to a breach of India’s obligation to provide an effective means of enforcing its rights.

The Tribunal did not accept that India had breached its fair and equitable treatment obligation. This was because White Industries had not done everything it could to prevent the delay.

Therefore, White Industries was awarded the amount due under the original ICC award plus interest dating from 2002 and costs. In other words, White Industries was awarded the amount it would have been entitled to but for the delays it faced in the Indian courts.

Where there is a BIT in existence between the host State in which your project is located and your own country, the decision in *White Industries v India* will provide additional support in attempts to enforce arbitral awards. Where other attempts to enforce or negotiate payment against an award have been exhausted, the threat of direct action against the host State Government may very well introduce new pressures which could lead to a satisfactory result.

### An Indian post-script

On 6 September 2012, in the case of *Bharat Aluminium Co. v Kaiser Aluminium Technical Service, Inc.*<sup>2</sup>, the Indian Supreme Court, a five-judge constitutional bench, held that the provisions of Part I of the Indian Arbitration Act 1996 have no application to international commercial arbitration proceedings conducted outside of India. This decision, which applies prospectively to all arbitration agreements executed after 6 September 2012, will serve to restrict the ability of local courts to interfere in international arbitrations seated outside India. The Honourable Justice Surinder Singh Nijjar, stated that awards rendered by international tribunals seated outside of India:

*“... would only be subject to the jurisdiction of the Indian courts when the same are sought to be enforced in India in accordance with the provisions contained in Part II of the Arbitration Act, 1996.”*

This should mean that the fact that the parties have chosen Indian law or that the dispute has connections with India (and that can be because a company is a local one or because the subject matter is inside India) will not, on its own, create jurisdiction for Indian courts to exercise supervisory jurisdiction over arbitration proceedings. For example, an application for interim relief (in the form of an injunction) cannot be brought pursuant to Part I of the Indian Arbitration Act 1996 in cases where the seat of arbitration is outside of India. Equally, if an international investor and an Indian company agree to refer disputes arising under a contract to international arbitration seated outside of India, neither party will be able to use the machinery in the Indian Arbitration Act 1996 to obtain an injunction from the Indian Courts so as to restrain those arbitration proceedings. On any major international project, it is always sensible to check whether, and if so, to what extent, the local courts might have the power to intervene.

*However, the Australia - India BIT contained what is known as a “most favoured nation” clause meaning that parties are able to make use of provisions in other BITs if the provisions of that other BIT gave investors of another nation greater protection.*

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<sup>2</sup> Civil Appeal No. 7019 of 2005

## Bonds and guarantees

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# Bonds and guarantees

*There have been a number of recent cases in relation to bonds and guarantees. Nicholas Gould provides an update as to what they mean.*

### Interpretation - on demand or guarantee?

The case of *Vossloh Aktiengesellschaft v Alpha Trains (UK) Ltd*<sup>1</sup> concerned a security document given by a parent company of the Vossloh Group. The guarantee related to the number of trains sold to the Alpha Group. The beneficiary claimed that the words “principal debtor and not merely as surety, as a separate, continuing and primary obligation” meant that the obligation was a primary obligation and not a secondary guaranteeing obligation.

The Judge did not agree. A mere assertion of a breach or failure to pay money was not sufficient. Reading the guarantee as a whole, it required there to be a default by the principal in performing the underlying contract or in making a payment of the sum due.

There is a presumption that an instrument is not a performance bond unless it is issued by a bank in the form of a banking instrument. Alpha had not rebutted that presumption. The mere use of the expression “on demand” was insufficient to establish that the guarantee was in fact “on demand”. Alpha Trains therefore had to establish liability in respect of the sum due before making a call on the bond.

In *Carey Value Added, S.L.B Groupo Urvasco SA*<sup>2</sup>, the High Court had to consider whether a security document was truly an on demand bond or a secondary guarantee obligation. The expression “all obligations of the Obligors under or in connection with the transaction documents” were co-extensive with the borrower’s liability. The guarantor was therefore responsible as primary obligor for any failure of the borrower. This did not amount to an immediate unconditional on demand bond.

The case of *Kookmin Bank v Rainy Sky SA & Others*<sup>3</sup>, considered the interpretation and scope of “all such sums due”. Six almost identical on demand advance payment bonds had been provided as security for obligations undertaken by a Korean ship builder in relation to six ship building contracts. The ship-builder later became insolvent, and so the beneficiary sought repayment of instalments that had been made. The bond was in respect of “all such sums due to you under the contract”.

The call on the bond was resisted on the basis that demands for instalments made were not sums due. The Court disagreed, holding that the word “such” should not be ignored. This word referred back to the sums in relation to the pre-delivery instalments under the ship building contract, as the purpose of the bond was to guarantee their repayments and nothing else.

### When is a primary obligor a bondsman or merely a guarantor?

In *Wuhan Guoyeu Logistics Group Co Ltd & Others v Emporiki Bank of Greece SA*<sup>4</sup>, the security document contained the phrase “as primary obligor”. Construing the document as a whole, it was a guarantee and not an on demand bond. The primary obligation was to pay the sum actually due in respect of the underlying contract, not to pay on first demand without demonstration of a debt.

### On demand unconditional bonds – resisting a call

It is important to remember that for an injunction to be granted, an applicant will need to show that it has a “seriously arguable” case, and also to follow the guidelines in *American Cyanamid Ethicon*<sup>5</sup>. This general principle for injunctions needs to be considered in the context of resisting on demand bonds, and further the identity of the party that can be effectively restrained.

*The mere use of the expression “on demand” was insufficient to establish that the guarantee was in fact “on demand”.*

*Construing the document as a whole, it was a guarantee not an on demand bond. The primary obligation was to pay the sum actually due in respect of the underlying contract, not to pay on first demand without demonstration of a debt.*

<sup>1</sup> [2010] EWHC 2443 (Ch)

<sup>2</sup> [2010] EWHC 1905 (Comm)

<sup>3</sup> [2010] EWCA Civ 582

<sup>4</sup> [2012] EWHC 1715 (Comm)

<sup>5</sup> [1975] AC 395

## Bonds and guarantees

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In addition, it might also be possible in limited circumstances to rely on the terms of the underlying contract, although the on demand bond is a primary obligation in its own right.

### Exceptions: fraud and underlying contract

In *Permasteelisa Japan KK v (1) Bouyguesstroi (2) Banca Intessa Spa*<sup>6</sup> Ramsay J held that a permanent injunction could only be provided in order to prevent a call on an on demand bond in very limited circumstances. One of the following has to be demonstrated:

- A “seriously arguable” case in respect of fraud; or
- A “positively established” breach of the underlying contract within the parties. Positively established means more than “seriously arguable”.

In the case of *Sirius International Insurance v FAI General Insurance*<sup>7</sup> the House of Lords held that it was possible to grant an injunction where the underlying contract expressly restricted a party's right to call upon a letter of credit. On demand bonds are sufficiently similar, and Ramsay J held in *Permasteelisa* that the same principle applied.

### The party to the fraud

The other question to consider is that if fraud is to be established then which party must have knowledge of the fraud:

- The Bank – an injunction will only be granted against a bank if there is a seriously arguable case that the person calling on it did not honestly believe the validity of the cause (*United Trading v Allied Arab Bank*<sup>8</sup>). The purpose of obtaining an injunction against a bank is to stop them paying money under the security documents.
- The Beneficiary – the court will only grant an injunction against a beneficiary if there is a “seriously arguable” case that the beneficiary could not honestly have believed in the validity of its own call on the document (*Intraco Ltd v Notis Shipping Corporation Bhoja Trader*<sup>9</sup>).
- Third parties by Freezing Order – the court may impose a freezing order on the money flowing from the performance guarantee (see once again *Bhoja Trader*, this time para 258).

### Relationship with the underlying contract

The security in *Simon Carves Ltd v Ensus UK Ltd*<sup>10</sup> was an on demand bond. It was held that the terms of the main contract governed when the bond was to expire. There was a “very strong case” that the bond had expired, and therefore the injunction continued. This is a rare case of an injunction continuing in relation to a call on an on demand bond; in this case because the underlying contract arguably demonstrated that the bond had expired.

Here, Mr Justice Akenhead confirmed that unless fraud is established, the court will not prevent a bank from paying out on a demand bond provided the conditions of the bond itself have been complied with (such as formal notice in writing). However, fraud is not the only grounds upon which a call on a bond can be restrained by injunction. The same principles apply in relation to a beneficiary seeking payment under the bond. There is no legal authority that permits a beneficiary to make a call on the bond when it is expressly disentitled from doing so.

If the underlying contract clearly and expressly prevents the beneficiary from making a demand under the bond, it can be restrained by the court from making a demand under the bond. The court did not need to make a final determination on whether the underlying contract prevented payment at the interim injunction stage. It only needed to satisfy itself that the party resisting the demand had a “strong case”. It cannot be expected that the court at that stage will make in effect what is a final ruling.

***Fraud is not the only ground upon which a call on a bond can be restrained by injunction. The same principles apply in relation to a beneficiary seeking payment under the bond. There is no legal authority that permits a beneficiary to make a call on the bond when it is expressly disentitled from doing so.***

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<sup>6</sup> [2007] EWHC 3508 (TCC)

<sup>7</sup> [2004] UKHL 54

<sup>8</sup> [2011] EWHC 657 (TCC)

<sup>9</sup> [1985] 2 Lloyd's 554

<sup>10</sup> [1981] 2 Lloyd's 256, at para 257

<sup>11</sup> [2012] EWCA Civ 265

<sup>12</sup> [2008] EWCA Civ 819

## Negotiating and concluding contracts by email

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# Negotiating and concluding contracts by email

*In the increasingly electronic world in which we all live and work, traditional rules, regulations and standards are coming under more and more scrutiny. In the UK, there have been a number of legal cases relating to the question of whether an email, or even the typing of a name at the bottom of an email is sufficient to amount to a binding contract. In March of 2012, the second highest appellate court, the Court of Appeal, had to consider<sup>1</sup> whether or not a contract of guarantee was enforceable when it was contained not in a single document signed by the guarantor but in a series of documents, including emails said to have been authenticated by the signature of the guarantor.*

***Before you press send, read your email through. Have you actually accepted or confirmed the terms (or some of them at least) you are meant to be negotiating?***

Although clearly a decision binding only under English law, the case raises a number of issues which are relevant to any contract negotiations. The dispute related to a claim by Golden Ocean under an alleged guarantee for some US\$57 million arising out of the alleged repudiation of a long term charter. In early 2008 Golden Ocean offered to charter to SMI (or an account guaranteed by SMI) a vessel with an option to purchase the vessel at the end of the charter period. The entity nominated by SMI to enter into the charter was Trustworth Shipping Pte Ltd. Trustworth was a related company. The negotiations following this offer were conducted by email and proceeded on the basis "Trustworth fully guaranteed by SMI." When disputes arose it was argued that the email chain was too disjointed and insufficient to constitute a guarantee. There was no single document that could be identified as the contract of guarantee. It was further said that the guarantee was unenforceable, under section four of the Statute of Frauds<sup>2</sup> provides:

*"No action shall be brought whereby to charge the Defendant upon any special promise to answer for the debt default or miscarriage of another person unless the agreement upon which such action shall be brought or some memorandum or note thereof shall be in writing and signed by the party to be charged therewith or some other person thereunto by him lawfully authorised."*

The original Judge, Mr. Justice Christopher Clarke had commented that as a matter of commercial good sense it was:

*"highly desirable that the law should give effect to agreements made by a series of e-mail communications which follow, more clearly than many negotiations between men of business, the sequence of offer, counter offer, and final acceptance, by which, classically, the law determines whether a contract has been made."*

Further, he held that the fact that the emails which constituted the contract were signed by the electronically printed signature of the persons who sent them was sufficient to constitute a signature for the purpose of the Statute of Frauds. His approach was followed by the Court of Appeal.

In the Court of Appeal, Lord Tomlinson looked at why there was a requirement that the agreement must be both in writing and signed by the guarantor. There was nothing in the Statute of Frauds containing an express indication that the agreement in writing must be in one or even a limited number of documents. The purpose of the requirement that the agreement must be both in writing and signed by the guarantor was not there to ensure that the documentation was economical. The reason was to ensure that the parties knew exactly what had been promised and to avoid ambiguity and the need to decide which side was telling the truth about whether or not an oral promise had been made<sup>3</sup>.

Further, the conclusion of commercial contracts by an exchange of emails<sup>4</sup>, in which the terms agreed at an early stage are not repeated later in the course of correspondence, is far from unusual. Whilst it may be more common and is certainly more convenient in commercial transactions for a contract of guarantee to be contained in a single document, it is today equally commonplace for charterparties, as it is for many different forms of contract to be concluded by an email exchange, and the parties here had no

<sup>1</sup> The case is *Golden Ocean Group Ltd v Salgaocar Mining Industries Pvt Ltd and Anr*, [2012] EWCA Civ 265.

<sup>2</sup> The Statute dates from 1677, a time when feather quills dipped in ink were the writing instrument of choice.

<sup>3</sup> Following Lord Hoffman in *Actionstrength Ltd v International Glass Engineering SPA* [2003] 2 AC 541.

<sup>4</sup> And it was not so long ago that you could substitute the fax for an email.

## Negotiating and concluding contracts by email

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difficulty in knowing at exactly what point they had undertaken a binding obligation and on what terms. In fact it was only necessary to look at two of the emails to identify a clear agreement. Lord Tomlinson said that:

*"The present case is not concerned with prescribing best or prudent practice. It is concerned with ensuring, so far as is possible, that the adoption of usual and accepted practice cannot be used as a vehicle for injustice by permitting parties to break promises which are supported by consideration and upon which reliance has been placed."*

It is often said that the parties are the masters of their contractual bargain. If the documents relied upon in making up a contract contemplate the execution of a further contract it becomes a question of construction as to whether the execution of that further contract is a condition of the bargain (in which case there will be no enforceable contract either because the condition is unfulfilled) or whether it is a mere expression of the desire of the parties as to the manner in which they would like to proceed (in which case provided there is a binding contract, the lack of a formal contract does not matter). The proposed guarantor could have made it clear that it was not to be bound until execution of a formal document, of whatever kind, but it did not do so. Equally, the owners too could have stipulated that they too were not to be bound until execution of a formal document. Neither party did so.

When it came to the signature, it was accepted that all that is required is that the guarantor's name is written or printed in the document<sup>5</sup>. The document here which confirmed the conclusion of the contract of guarantee was an email ending with the name Guy, indicating that it was sent by Mr. Hindley, the broker. It was suggested that this was not a signature at all. It was no more than a salutation, and it was certainly not a signature appropriate or effective to authenticate a contract of guarantee.

In the view of the court, by putting down his name at the end of the email, Mr. Hindley indicated that the email duly came with his authority and that he took responsibility for the contents. Further, professional brokers understand that their communications give rise to obligations binding their principals. This was not simply an inconsequential communication. It was a communication which the brokers will readily have appreciated brought into being both the charterparty and the guarantee. It was therefore sufficient to act as a signature as required by the Statute of Frauds.

Indeed, if you think about it, not everyone when they sign their name, actually sets out their name in full. Some use just one word, others the four or five that make up their entire name. In the world of today, why should it be so different when you type your full name or just your first? Some people have electronic signatures which replicate their written one. Remember that all can be equally binding.

### So what can you do?

We all do business by email. First of all, remember that an email (as quite probably is a text if you regularly use sms in the course of your business dealing) is the equivalent of a letter. Second, if you are negotiating by way of email, you may want to take a cautious approach and mark your emails "subject to contract,"<sup>6</sup> or perhaps some other condition. For example, it may be that final agreement will not be made unless and until the parties have signed a formal final document.

Thirdly, before you press send, read your email through, have you actually accepted or confirmed the terms (or some of them at least) you are meant to be negotiating? Remember too, that if you start performing the contract before the formal terms are agreed (and there are often pressing commercial reasons why this is so, whatever the lawyer may say) then you may find that you are left with a contract that is only partially agreed. It may be that in the future, a dispute arises over one of the grey areas that were left unresolved. Keep a checklist, so you know what is and is not agreed. And finally, of course, and it is easier said than done – just check who you are actually sending your email to.

*It is "highly desirable that the law should give effect to agreements made by a series of e-mail communications which follow, more clearly than many negotiations between men of business the sequence of offer, counter offer, and final acceptance, by which, classically, the law determines whether a contract has been made."*

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<sup>5</sup> Indeed, following *WS Tankship II BV v The Kwangju Bank Ltd & Anr* [2011] EWHC 3103 (Comm) the words "Kwangju Bank Ltd" which were contained in the header to the SWIFT message from a bank was a sufficient signature for the purposes of the Statute of Frauds. The words "Kwangju Bank Ltd" appeared in the header, because the bank caused them to be there by sending the message. Whether or not automatically generated by the system, and whether or not stated in whole, or abbreviated this was a sufficient signature.

<sup>6</sup> Although remember that simply adding the words "subject to contract" may not be enough. It is not just the title given to a letter it is how you are acting that counts. If the parties by their correspondence are acting inconsistently with the subject to contract designation, the protection will fall away.

## Concurrency, global claims and loss and/or expense

# Concurrency, global claims and loss and/or expense

*The case of Walter Lilly and Co Ltd v Mackay<sup>1</sup> was described by Mr Justice Akenhead as being “a full-blooded conflict between the parties in which there seems to have been little, no or belated room for compromise.” The judgment that resulted has provided valuable guidance on the preparation and likely resolution of claims, including in relation to the correct approach to determining extension of time claims (in England and Wales) where there is concurrency, global claims and the nature of information contractors are required to provide when submitting claims, at least under the JCT Form.*

Walter Lilly was engaged by DMW in 2004 as a main contractor under a JCT Standard Form of Building Contract with bespoke amendments to build three houses at 1, 2 and 3 Boltons Place, Earls Court. Mr and Mrs Mackay were to occupy number 3 on completion. Mr Mackay (together with Mr Daniel and Mr West, who were to occupy numbers 2 and 3) formed DMW as the corporate vehicle through which the development would be carried out. Little, if any of the design had been completed prior to the involvement of WLC, as a result of which the project suffered from considerable delay.

*“..where there is an extension of time clause such as that agreed upon in this case, and delay is caused by two or more effective causes, one of which entitles the contractor to an extension of time as being a relevant event, the contractor is entitled to a full extension of time.”*

### Concurrent delay

Upon commencement of the project, DMW and WLC agreed to split the building contract in three so that there would be a separate contract for each plot. A deed of variation dated 23 December 2004 was signed to this effect. Throughout the project period WLC had sought, and was granted, extensions of time on numerous occasions by the first architect under the building contract. DMW eventually changed architect and at the date of practical completion (deemed by the court to have occurred on 7 July 2008) DMW withheld liquidated damages for late completion. WLC argued that it was entitled to an extension of time for the whole period of delay. DMW said that WLC was responsible for the delays. Mr Justice Akenhead notably distinguished between a prospective assessment of delay by the architect before practical completion occurs and a retrospective analysis by a court, arbitrator or the architect after practical completion.

Following this approach, the Judge found that the court must use its knowledge of events as provided by witness and expert evidence, and on the balance of probabilities should determine what delay was actually caused by relevant events. The relevant extension of time clause required the Architect to grant an extension of time which was “fair and reasonable having regard to any of the Relevant Events.” There was nothing in the extension of time clause, which was in standard form, to suggest that any extension of time should be apportioned or reduced if the Contractor could be shown to have been partly responsible for the delay. It should also be remembered that the relevant events tend to be matters for which the employer is responsible. Having considered a number of English authorities on concurrent delay, including *Henry Boot Construction (UK) Ltd v Malmaison Hotel (Manchester) Ltd* and the more recent decision in *Adyard Abu Dhabi v SD Marine*,<sup>2</sup> the Judge held that WLC was entitled to the full extension of time claimed:

*“where there is an extension of time clause such as that agreed upon in this case, and delay is caused by two or more effective causes, one of which entitles the contractor to an extension of time as being a relevant event, the contractor is entitled to a full extension of time.”*

In reaching his conclusion, while recognising the judgment as “persuasive”, the Judge notably rejected the approach taken by the Scottish court in *City Inn Ltd v Shepherd Construction Ltd*<sup>3</sup> as “being inapplicable in this jurisdiction”.

### Global claims

Here, Mr Justice Akenhead again reviewed a number of the traditional authorities including the *Crosby*, *Merton*, *Wharf*, *Stockley Park* and *John Doyle* cases and concluded that there is nothing in principle “wrong” with a “total” or “global” cost claim.

<sup>1</sup> [2012] EWHC 1773 (TCC)  
<sup>2</sup> [1999] 70 Con LR 32 and [2011] EWHC 848  
Comm  
<sup>3</sup> [2010] BLR 473



## Concurrency, global claims and loss and/or expense

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Claims by contractors for delay or disruption related to loss and expense must be proved as a matter of fact. The contractor has to demonstrate on a balance of probabilities that, first, events occurred which entitle it to loss and expense; secondly, that those events caused delay and/or disruption; and thirdly, that such delay or disruption caused it to incur loss and/or expense (or loss and damage as the case may be). It does not, as a matter of principle, have to be shown by a claimant contractor that it is impossible to plead and prove cause and effect in the normal way or that such impossibility is not the fault of the party seeking to advance the global claim. In the absence of any contractual restrictions, the claimant contractor simply has to prove its case on a balance of probabilities.

There is no set way for contractors to prove their claim. It can be done with whatever evidence will satisfy the tribunal and the requisite standard of proof. The Judge noted that a claim may be supported or even established by detailed factual evidence which precisely links reimbursable events with individual days or weeks of delay or with individual instances of disruption, which then demonstrates with precision to the nearest penny what that delay or disruption actually cost.

### What does a contractor have to prove?

A global claim may have added evidential difficulties which a claimant contractor has to overcome. For example, it will generally have to establish (on a balance of probabilities) that the loss that it has incurred (namely the difference between what it has cost the contractor and what it has been paid) would not have been incurred in any event. This means it will need to demonstrate that its accepted tender was sufficiently well priced that it would have made some net return.

It will also need to demonstrate in effect that there are no other matters that actually occurred (other than those relied upon in its pleaded case and which it has proved are likely to have caused the loss). However, it was wrong to suggest that the burden of proof transfers to the defending party. That said, the defending party can raise issues, or adduce evidence, that suggest or even show that the accepted tender was so low that the loss would always have occurred irrespective of the events relied upon by the claimant contractor or that other events (which are not relied upon by the claimant as causing or contributing to the loss or which are the "fault" or "risk" of the claimant contractor) occurred which may have caused or did cause all or part of the loss.

The fact that one or a series of events or factors (unpleaded or which are the risk or fault of the claimant contractor) caused or contributed (or cannot be proved not to have caused or contributed) to the total or global loss does not necessarily mean that the claimant contractor can recover nothing. The Judge gave as an example, the situation where a contractor's global loss is £1 million and it can prove that but for one overlooked and unpriced £50,000 item in its accepted tender it would probably have made a net return; the global loss claim does not fail simply because the tender was underpriced by £50,000. The consequence would simply be that the global loss is reduced by £50,000 because the claimant contractor has not been able to prove that £50,000 of the global loss would not have been incurred in any event.

If there are events during the course of the contract that are the fault or risk of the claimant contractor and which caused or cannot be demonstrated not to have caused some loss, the overall claim will not be rejected save to the extent that those events caused some loss. Here the Judge gave an example of time spent by management in dealing with lift problems (in particular over-cladding). Assuming that this time can be quantified either precisely or at least by way of assessment, that amount would be deducted from the global loss. Mr Justice Akenhead noted that this was not inconsistent with the Judge's reasoning in the *Merton* case that "a rolled up award can only be made in the case where the loss or expense attributable to each head of claim cannot in reality be separated", because, "where the tribunal can take out of the "rolled up award" or "total" or "global" loss elements for which the contractor cannot recover loss in the proceedings, it will generally be left with the loss attributable to the events for which it is entitled to recover loss".

*Whilst there is nothing in principle "wrong" with a global claim, it may raise evidential difficulties since the contractor will have to show that the loss he has incurred would not have been incurred in any event.*

## Concurrency, global claims and loss and/or expense

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There is no need for the court to go down the global or total cost route if the actual cost attributable to individual loss-causing events can be readily or practicably determined. However, the suggestion that a global award should not be allowed where the contractor himself has created the impossibility of disentanglement was, in the view of the Judge, wrong. And not, as had been argued in the *Walter Lilly* case supported by either the *Merton* or *John Holland* cases. Mr Justice Akenhead noted that in *Merton*, Vinelott J was referring to unreasonable delay by the contractor in making its loss and/or expense claim; that delay would have led to their being non-compliant with the condition precedent but all that he was saying otherwise was that, if such delay created difficulty, the claim may not be allowed. Vinelott J was not saying that a global cost claim would be barred necessarily or at all if there was such delay. In *John Holland*, Byrne J relied on Vinelott J's observations. Again he did not say that a global cost claim would be barred but simply that such a claim "has been held to be permissible in the case where it is impractical to disentangle that part of the loss which is attributable to each head of claim, and this situation has not been brought about by delay or other conduct of the claimant".

This all led Mr Justice Akenhead to conclude that:

*"In principle, unless the contract dictates that a global cost claim is not permissible if certain hurdles are not overcome, such a claim may be permissible on the facts and subject to proof."*

*"In my judgment, it is necessary to construe the words in a sensible and commercial way that would resonate with commercial parties in the real world."*

### Will a global claim succeed at trial?

This leaves open the question of whether a global claim will succeed at trial. At trial, it should not be forgotten that you must prove your case and there is an important distinction between a global claim as a matter of pleading and a global claim as a matter of evidence. The position seems to be this:

- Where a claim for an extension of time and/or loss and expense is advanced pursuant to contractual terms, then an arbitrator or the court can make a global award, subject to the same limitations as were set out in the *Walter Lilly* case. This means that whilst a tribunal will be more sceptical about the global cost claim if the direct linkage approach is readily available but is not deployed, that does not mean that the global cost claim should be rejected out of hand. That said, the mood is against merely impressionistic assessments, and a claimant is far more likely to succeed if he can show what effects flowed from what events giving rise to entitlement.
  - Where the claim is for damages for breach of contract, the claimant's task may be somewhat easier, because he will usually be able to claim damages for loss of a chance, at any rate in the alternative, and under that head the arbitrator or the court is much more likely to be persuaded - indeed is probably required - to take an impressionistic approach.
  - Contractors must prove their claims as a matter of fact and on the balance of probabilities. They must show the occurrence of a Relevant Event and that it caused delay leading to loss and expense. In principle, a contractor does not need to show, when putting forward a global claim, that it is impossible to plead and prove cause and effect in the normal way. If there are contractual restrictions on global claims, then they may have an impact. Otherwise, the contractor must prove his case on the balance of probabilities.
  - Whilst there is nothing in principle "wrong" with a global claim, it may raise evidential difficulties since the contractor will have to show that the loss he has incurred would not have been incurred in any event. He will need to demonstrate that his tender was sufficiently well priced that he would have made some net return and that no other matters are likely to have caused the loss. A global claim does not transfer the burden of proof to the party defending it and he may adduce evidence that the accepted tender was so low that the loss would always have occurred, irrespective of the events relied on by the contractor.
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## Concurrency, global claims and loss and/or expense

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- Even if an event that is not the fault of the employer caused or contributed to the global loss, that does not mean that the contractor will recover nothing. It depends on the impact of such an event. It may be that the claim will not be rejected but a deduction will be made for the individual event which is not the employer's responsibility.
- If it is practicable to attribute actual costs to individual events, the court may be sceptical about a global claim. However, a global award may be made even if the contractor himself created the impossibility of disentanglement as to the various causes. The measure of the claim's success will depend on the facts and will be subject to proof.

### Loss and expense/notification of claims

The Judge also had to consider Walter Lilly's claims for loss and expense which were subject to the standard JCT loss and expense clause. The relevant clause was based on the standard JCT clause 26.1 (the JCT 2011 equivalent is 4.23) which said that:

- 26.1.1, the contractor's application shall be made as soon as it has become, or should reasonably have become, apparent to him that the regular progress of the Works or of any part thereof has been or was likely to be affected as aforesaid; and
- 26.1.2, the contractor shall in support of his application submit to the architect such information as should reasonably enable the architect to form an opinion as aforesaid; and
- 26.1.3, the contractor shall submit to the architect or to the quantity surveyor such details of such loss and/or expense as are reasonably necessary for such ascertainment as aforesaid.

*The architect must be satisfied that the loss and expense claimed is likely to be or has been incurred but he does not have to be "certain".*

The Judge noted that an entitlement to various heads of loss and expense will not be lost where for some of the loss details are not provided. Otherwise, one can have the absurd position that where £10 out of a £1 million claim is not adequately detailed but the rest of the claim is, the whole claim would fail to satisfy the condition precedent. That cannot have been intended. The condition precedent within clause 26.1.3 only requires the contractor to submit details which "are reasonably necessary" for the ascertainment of loss and expense. It does not say how the details are to be provided but there is no reason to believe that an offer to the architect for them to inspect records at the contractor's offices could not be construed as submission of details of loss and expense.

What is required is "details" of the loss and expense and that does not necessarily include all the backup accounting information that might support such detail. It would have been possible for the clause to say that the contractor should provide "details and all necessary supporting documentation" but that is not what the clause says. There is no need to construe clause 26.1.3 in a peculiarly strict way or in a way which is penal as against the contractor, particularly bearing in mind that all the clause 26.2 grounds that give rise to the loss and expense entitlements are the fault and risk of the employer. The architect must be satisfied that the loss and expense claimed is likely to be or has been incurred but he does not have to be "certain".

In accordance with *London Borough of Merton v Leach*, it is legitimate to bear in mind that the architect is not a stranger to the project in considering what needs to be provided to them. For example, they almost certainly attend site meetings. The obligation is to submit details which are "reasonably necessary" for the ascertainment of loss and expense. The Judge noted that the word "ascertain" means to determine or discover definitely or, more archaically, with certainty. This did not mean that, the contractor had to produce every piece of conceivable material evidence such as was necessary to prove its claim beyond reasonable doubt:

*"In my judgment, it is necessary to construe the words in a sensible and commercial way that would resonate with commercial parties in the real world."*

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<sup>4</sup> (1985) 32 BLR 68

## Duties of project managers and contract administrators

# The duties of project managers and contract administrators

*It used to be thought that, because the project or construction manager himself did not undertake any work, his risk was modest. There were many reasons for this. Typically, his obligation is not an absolute one, partly because there is usually someone else to blame, and partly because of the difficulty that a claimant employer has in showing how matters would otherwise have turned out. However, there have been a handful of cases where this orthodoxy has been challenged. Two of these cases were reported in 2012. In one the project manager was found liable in circumstances where no formal contract was executed; in the other an employer's agent was not found to be under an absolute obligation to ensure that a contractor provided a bond.*

### *The Trustees of Ampleforth Abbey Trust v Turner & Townsend Project Management Ltd<sup>1</sup>*

Disputes arose between Ampleforth College and their contractor Kier Northern, which were settled through mediation. The project manager was TTPM. HHJ Keyser QC noted that there was an implied term of the contract between the Trust and TTPM that TTPM would exercise reasonable care and skill. Following the "Bolam test",<sup>2</sup> that duty is: "the standard of the ordinary skilled man exercising and professing to have that special skill". The Judge also noted that it may be impossible in any event, to define with precision the expression "project manager". In general terms, a project manager will act as the representative of the employer for the purpose of co-ordinating the different aspects of a construction project. Here, there was no dispute that TTPM was engaged to perform the full range of duties of a project manager, and these included facilitating, assisting and being involved in the procurement of the building contractor and the building contract.

During the project, the works were carried out under various letters of intent. This meant that Ampleforth had not been able to claim any liquidated damages for delay against Kier. The Trust did not contend that TTPM was wrong to advise that the works be commenced under a letter of intent; it was accepted that, in view of the perceived importance of achieving early completion and, specifically, early commencement of the works, it was acceptable to advise commencing the works under a letter of intent rather than waiting until a formal building contract could be executed. However, the Trust argued that TTPM should have advised the Trust:

- (i) Of the limited protection afforded to it by letters of intent as compared with an executed contract, in particular with regard to the availability of liquidated damages and the possibility of holding Kier liable for design defects;
- (ii) Of the increasing risk that the repeated issue of letters of intent would make it less likely that Kier would execute the contract; and
- (iii) Of the need to take resolute action to procure the execution of the contract by:
  - (a) taking positive action to remove specific obstacles, (b) identifying, by list, all outstanding matters and maintaining constant pressure on Kier to address them; (c) bringing commercial pressure to bear at a senior level; (d) threatening to withhold payment until all the outstanding matters had been dealt with; (e) threatening not to issue further letters of intent.

The Judge noted that in the performance of TTPM's role as co-ordinator and guardian of the client's interests:

*"efforts to finalise the contractual arrangements were of central importance. The execution of a contract is to be seen not as a mere aspiration but rather as fundamental. It is the contract that defines the rights, duties and remedies of the parties and that regulates their relationships. Standard-form contracts, such as the JCT contracts, are precise, detailed and structured*

*"Letters of intent are contracts of a skeletal nature; they pave the way for the formal contract, once executed, to apply retrospectively to the works they have covered,... They do not protect, and are not intended to protect, the employer's interests in the same manner as would the formal contract; that is why their "classic" use is for restricted purposes."*

<sup>1</sup> [2012] EWHC 2137 (TCC)

<sup>2</sup> *Bolam v Friern Hospital Management Committee* [1957] 1 WLR 583.

## Duties of project managers and contract administrators

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*documents; their elaborate nature reflects the complexities of the projects to which they relate and attempts to address the many and varied problems that can arise both during the execution of the works and afterwards. By contrast, letters of intent such as those used in the present case are contracts of a skeletal nature; they pave the way for the formal contract, once executed, to apply retrospectively to the works they have covered, but they expressly negative the application of most of the provisions of the formal contract until it has been executed. They do not protect, and are not intended to protect, the employer's interests in the same manner as would the formal contract; that is why their "classic" use is for restricted purposes."*

***Was a professional's obligation to "arrange" for a performance bond to be provided as part of the contract documents for the project an absolute obligation?***

HHJ Keyser QC held that TTPM was not under any absolute obligation to procure the execution of a formal contract. However, even if the outcome in this case (a project carried on from start to finish without an executed contract) did not of itself dictate the conclusion that TTPM was negligent, it was sufficient to suggest that something went wrong with the project. First, the evidence showed that it is extremely unusual for a building project of this scale to proceed from commencement to completion pursuant to letters of intent. Why, then, was no contract signed? To suggest that a contract should have been in place no later than April 2004 was hardly to suggest unreasonable haste. Works had started in early December 2003; by the expiry of the fourth letter of intent construction had been going on for about four months, and the works covered by the letters of intent accounted for more than 25% of the contract price.

### ***Sweett (UK) Ltd v Michael Wright Homes Ltd<sup>3</sup>***

MWH engaged Sweett to act as the employer's agent and provide quantity surveying services for a housing development. It was an express term of Sweett's appointment that they would: *"Prepare contract documentation and arrange for such documents to be executed by the parties hereto."*

Sweett made it clear to the contractor during pre-contract negotiations that a performance bond was required and ultimately it was an express term of the building contract that a bond would be provided. Despite numerous attempts by Sweett to secure the bond, the contractor failed to provide the bond. As a result of unpaid fees, Sweett terminated its agreement with MWH. In September 2008 Sweett commenced proceedings. The parties settled all aspects of the claim, save for MWH's counterclaim in respect of Sweett's failure to secure the bond. The contractor then went into liquidation in June 2009. The principal issue before the county court was whether Sweett had acted in breach of its duty in relation to the provision of a performance bond by the contractor.

MWH argued that either Sweett owed an absolute obligation to ensure that the performance bond was provided by the contractor or, even if there was no absolute obligation, Sweett still had a duty to take reasonable care to see that the bond was provided by the contractor. MWH further argued that Sweett should have at least withheld payment from the contractor in order to apply pressure on them to provide the bond. Sweett argued that there was no absolute obligation to ensure that the contractor provided the bond. Its sole obligation was to take reasonable care to ensure that the performance bond was provided, and that by making numerous requests to the contractor they had successfully discharged this obligation.

HHJ Wildblood QC held that Sweett did not owe an absolute duty to ensure that the contractor provided the bond. He considered the definition of "arrange" and found that Sweett's obligation stopped short of the requirement to "ensure". Provided it put in place the necessary steps for the bond to be executed (which on the evidence it did) Sweett would effectively have discharged its duty to "arrange" and therefore any breach would be limited to the consultant's common law duty to exercise reasonable skill and care.

Here the court noted in particular, the extensive steps that Sweett took to try and secure the bond. These included attending several meetings with both MWH and the contractor, and chasing the contractor for updates on a regular basis. This was sufficient to discharge the duty to "arrange" and to act with reasonable skill and care.

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<sup>3</sup> [2012] EW Misc 3 (CC)

## Best and reasonable endeavours clauses

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# Best and reasonable endeavours clauses

*Contracts in a construction context often contain “best” or “reasonable endeavours” or even “all reasonable endeavours” clauses. There have been a number of recent decisions where the courts have had to consider quite what these obligations require of those who sign up to them.*

Best endeavours' clauses make it clear that a best endeavours provision is sufficiently certain to be enforceable. Essentially such an obligation imposes a duty to do what can reasonably be done in the circumstances. Best endeavours means what it says - it does not mean second best endeavours. A party required to use its best endeavours is afforded less discretion and must, bar some qualifications, “leave no stone unturned”<sup>1</sup> in its attempts to comply. However, equally, it is not the “next best thing to an absolute obligation or a guarantee.”<sup>2</sup> The whole purpose of using the term is to qualify the obligation under the contract. That said, the extent to which the obligation is qualified will depend on the wording used, as well as the circumstances of the particular case. What matters is the commercial context and intentions of the parties.

It is usually thought that reasonable endeavours is less onerous than best endeavours. The Court of Appeal in *UBH (Mechanical Services) v Standard Life Assurance*<sup>3</sup> concluded that the exercise of reasonable endeavours involves a “balancing act whereby [the obligor] is obliged to put in one scale the weight of their contractual obligation to [the other party], and in the other they [are] entitled to place all relevant commercial considerations.” Relevant commercial considerations were held to include: relationships with third parties; the obligor's reputation; the cost incurred by the obligor; and the chances of achieving the desired result. Whilst the expected actions of the obligor are dependent on the individual circumstances of the case, an obligation to use reasonable endeavours will not require the obligor to “sacrifice its own commercial interests”. One exception to this is that where the contract actually specifies that certain steps have to be taken as part of the exercise of reasonable endeavours, those steps will have to be taken, even if that could be said to involve the sacrificing of the commercial interests of a party.

In the case of *CPC Group Ltd v Qatari Diar Real Estate Investment Company*,<sup>4</sup> the court was asked to consider the meaning of a slightly differently worded obligation to use “all reasonable but commercially prudent endeavours.” This, according to Mr Justice Vos, was not the equivalent to a “best endeavours” obligation and the clause did not require QDREIC to ignore or forgo its commercial interests. Instead, the clause allowed QDREIC to consider its own commercial interests alongside those of CPC, and required it to take all reasonable steps (here to procure the planning permission), provided those steps were commercially prudent.

### *Jet2.com Ltd v Blackpool Airport Ltd*<sup>5</sup>

In 2012, the Court of Appeal came to a slightly different conclusion, holding that an obligation to use “all reasonable endeavours” could include an obligation to act against your own commercial interests. A party under an obligation to use “all reasonable endeavours” cannot necessarily use cost or inconvenience as a grounds for not doing something where performance is under its control and does not depend on cooperation from a third party. The case arose out of a 15-year agreement for the operation of flights out of Blackpool Airport. Clause 1 of the Agreement stated that “Jet2 and BAL will co-operate together and use their best endeavours to promote Jet2's low cost services from Blackpool Airport and BAL will use all reasonable endeavours to provide a cost base that will facilitate Jet2's low cost pricing.”

There was nothing in the agreement about the scheduling of Jet2's flights and the times at which these could take place. However, with the support and cooperation of BAL for 4 years, Jet2 operated flights outside of the airport's published operating hours. By allowing departures outside hours the airport ran at a loss. On 22 October 2010, BAL told Jet2 that from midnight on 29 October 2010 it would not accept departures or arrivals scheduled outside normal hours. Jet2 obtained an injunction, and sought a declaration from the court that BAL was required under the agreement to allow Jet2 to run its previous operating hours. BAL said that the

*Although it is not a guarantee, a party required to use its best endeavours must “leave no stone unturned.”*

<sup>1</sup> *Sheffield District Railway Co v Great Central Railway Co* [1911] 27 TLR 451

<sup>2</sup> *Midland Land Reclamation Ltd & Anr v Warren Energy Ltd* [1997] CILL 1222

<sup>3</sup> [1986] TLR 13 November

<sup>4</sup> [2010] EWHC 1535

<sup>5</sup> [2012] EWCA Civ 417

## Best and reasonable endeavours clauses

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provisions of the Agreement that obliged it to cooperate and use best endeavours to promote Jet2's low cost services from the airport and to use all reasonable endeavours to provide a costs base that would facilitate Jet2's low-cost pricing did not require it to act against its own commercial interests. However, BAL also argued that its duties to use best or all reasonable endeavours did not require it to act against its own commercial interests (i.e. by running the airport at a loss). HHJ Mackie QC held that BAL was in breach of contract in refusing to handle flights outside of normal operating hours. This was a low-cost airline operation. BAL did not have the freedom to consider its own commercial interests in performing its endeavours duties. However, he did not grant Jet2 the declaration that aircraft movements should be allowed between 6 a.m. and midnight. In the context, it was "improbable" that the clause could be interpreted by the parties:

*"to mean that one of them could limit or abandon performance once it became commercially undesirable or unprofitable, just the sort of risks that parties expect to undertake when they contract. Any such unusual provision would have to be explicit before being accepted as part of what had been agreed."*

BAL appealed, arguing that clause 1 was vague and uncertain. It was a statement of aspiration. It had not been intended to create legal rights and obligations. For example, in *Little v Courage*, Millett LJ had stated:

*"An undertaking to use one's best endeavours to obtain planning permission or an export licence is sufficiently certain and is capable of being enforced; an undertaking to use one's best endeavours to agree, however, is no different from an undertaking to agree, to try to agree or to negotiate with a view to reaching agreement; all are equally uncertain and incapable of giving rise to an enforceable obligation."*

Jet2 said the parties had taken it for granted that it would need to schedule aircraft movements outside normal opening hours and that, by using its best endeavours to promote Jet2's business, BAL would ensure that it could do so. By a majority, the Court of Appeal agreed. The key difference was between a clause whose content is so uncertain that it is incapable of creating a binding obligation and a clause that gives rise to a binding obligation, the precise limits of which are difficult to define in advance but which can nonetheless be given practical content. Moore-Bick LJ confirmed that generally:

*"an obligation to use best endeavours, or all reasonable endeavours, is not in itself regarded as too uncertain to be enforceable provided that the object of the endeavours can be ascertained with sufficient certainty."*

Applying this principle to the facts of the case, the majority held that the object of the "best endeavours" obligation to promote Jet2's business was not too uncertain and therefore placed a binding obligation on BAL which extended to accepting departures and arrivals outside of the airport's normal operating hours. Lewison LJ, who disagreed with the majority, held that the endeavours duty was unenforceable for uncertainty. He noted:

*"It is... possible for a commercial organisation to undertake a positive commitment to run a business for a period as long as 15 years. It is even possible for such an organization to undertake a positive commitment to run a loss-making business for that period. But it would, I think, be an unusual obligation; and a businessman would expect such an obligation to be spelled out in clear words."*

The majority also agreed that the obligation to use all reasonable endeavours obliged BAL to act against its own commercial interests, holding that the losses incurred by BAL had not justified its actions. Whether, and if so to what extent, a person who has undertaken to use his best endeavours can have regard to his own financial interests will depend very much on the nature and terms of the contract in question. Here, the ability to schedule aircraft movements outside normal hours was essential to Jet2's business and was therefore fundamental to the agreement. In those circumstances one would not expect the parties to have contemplated that BAL should be able to restrict Jet2's aircraft movements to normal hours simply because it incurred a loss each time it was required to accept a movement outside those hours, or because keeping the airport open outside normal hours proved to be more expensive than it had expected. On the other hand, there was force in the argument that if it became clear that

***"... an obligation to use best endeavours, or all reasonable endeavours, is not in itself regarded as too uncertain to be enforceable provided that the object of the endeavours can be ascertained with sufficient certainty."***

## Best and reasonable endeavours clauses

Jet2 could never expect to operate low-cost services from Blackpool profitably, BAL would not be obliged to incur further losses seeking to promote a failing business. LJ Longmore stated:

*“the fact that [a party] has agreed to use his best endeavours pre-supposes that he may well be put to some financial cost, so financial cost cannot be a trump card to enable him to extricate himself from what would otherwise be an obligation.”*

### *Ampurius Nu Homes Holdings Ltd v Telford Homes (Creekside) Ltd*<sup>6</sup>

Telford, a developer, agreed to build and develop four properties and grant long leases of the commercial units to Ampurius. Although work started promptly on the construction, in March 2009 Telford decided that it would be necessary to put work on Blocks A and B on hold because of funding difficulties. Work on those blocks did not resume until early October 2010. Ampurius sought to terminate the contract by letter from its solicitors dated 22 October 2010 on the basis of repudiatory breach by Telford. Telford itself terminated the contract on 9 November 2010 following non-payment by Ampurius of monies said to be due. There was no termination clause in the contract, although Telford agreed to use its reasonable endeavours to procure completion of the Works by the Target Date or as soon as reasonably possible thereafter.

The Judge found that Telford were in breach because they had stopped work, something which was contrary to the obligation to proceed with due diligence. Strictly, this meant that the Judge did not need to consider the question of reasonable endeavours. Telford had submitted that the expression encompassed financial resources, so that if Telford could not complete by the Target Dates because of its funding problems, it would not be in breach so long as it had made reasonable endeavours to procure finance. The project was blighted by the failure of Lehman Brothers just after the execution of the agreement. The Judge accepted that Telford had done all that could reasonably be done in that regard. However, the Judge did not:

*“think that a ‘reasonable endeavours’ clause as regards the time of completion in what is, in this respect, a construction contract can extend to endeavours to have sufficient money to perform the contract. Although the language could literally bear that meaning, in my judgment, on an objective reading the qualification of “reasonable endeavours”, as opposed to an absolute obligation to complete, is designed to cover matters that directly relate to the physical conduct of the works, thereby providing an excuse for delay in such circumstances as inclement weather or a shortage of materials for which the Defendant was not responsible. The clause does not, in my view, extend to matters antecedent or extraneous to the carrying out of the work, such as having the financial resources to do the work at all.”*

### Conclusions

That a party cannot rely on its own financial difficulties to excuse failure to use reasonable endeavours is perhaps not unexpected and reflects the approach the courts have taken to claims that a contract has been frustrated or otherwise suspended due to the financial crisis.<sup>7</sup> However, these cases demonstrate that best or reasonable obligations can create uncertainty as to what exactly is required of a party to a contract. As with any obligation, the more precise the endeavours clause in a contract, the less likely it is to lead to disputes. Whilst the courts are willing to uphold an endeavours clause especially where a contract is already being performed, in order for it to be valid, the parties need to be clear on its objective. If not then the clause may not be enforceable.

However, when it comes to acting against one's commercial interests, it is clear that what a particular party should do to comply with a 'best endeavours' obligation will depend on the context of the clause and the factual background. Therefore, where possible, parties might want to consider whether it is practical or possible to specify the steps a party is required to take (or not take) in order to comply with an obligation. This could be done by setting criteria by which a party's endeavours can be assessed. Care should be taken to record any steps that are taken to comply with the obligation. Remember too that any change in approach might be taken to be evidence that the clause is no longer being complied with.

*“An objective reading the qualification of “reasonable endeavours”, as opposed to an absolute obligation to complete, is designed to cover matters that directly relate to the physical conduct of the works, thereby providing an excuse for delay...[for matters] for which the Defendant was not responsible. The clause does not...extend to matters antecedent or extraneous to the carrying out of the work, such as having the financial resources to do the work at all.”*

<sup>6</sup> [2012] EWHC 1820 (Ch)

<sup>7</sup> See *Thames Valley Power v Total Gas & Power* [2006] 1 Lloyd's Rep 441



## Dictionary

# Dictionary of construction terms

*Fenwick Elliott's Dictionary of Construction Terms is published at the end of 2012. It offers clear and concise explanations of the most common legal and technical terms, phrases and abbreviations used throughout the construction industry. In addition to offering thorough coverage of frequently-used terms, this practical dictionary also includes details of legal and technical acronyms, drawings and diagrams to illustrate both legal and technical terms and terminology relating to common institutions. We set out some example definitions below.*

*The Fenwick Elliott Dictionary of Construction Terms is intended to provide a dependable and trustworthy guide to construction industry terminology. It is unique in its broad and authoritative coverage of the subject area and provides a user-friendly and convenient reference for those in the construction industry.*

**Call-off contract** A contract, usually for a fixed period of time, made with one or more contractors, suppliers or service providers for a defined range of works, goods or services covering terms and conditions (including price). Typically an individual contract is awarded or called off under a **Framework Agreement** for the provision of the particular services, goods or works in question.

**Candela** A standard unit of luminous intensity in the International System of Units (SI).

**Canons of construction** Established rules which are applied in construing a document to arrive at its legal effect.

**Cantilever** A beam or other horizontal member which is fixed only at one end - **Figure C1**

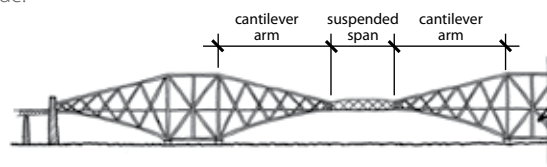
**Capacity** The ability of a person or other legal entity to enter into a binding contract. Generally, certain classes of people or entities cannot enter into a binding contract, such as minors, agents unless their terms of appointment entitle them to do so, unincorporated associations and persons suffering from mental illness or learning difficulties.

**Caparo Industries v Dickman** [1990] UKHL 2: the House of Lords put forward a threefold test to establish whether a duty of care is owed by one party to another in tort. The test seeks to establish whether the damage which occurred was foreseeable; whether there is sufficient proximity in the relationship between the parties; and finally, whether it is just, fair and reasonable in all the circumstances to impose a duty of care.

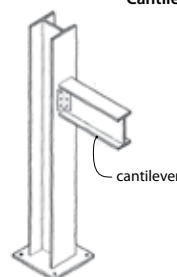
**Capillary action (Capillarity)** The tendency of a liquid to rise in narrow tubes or to be drawn into small openings such as those between grains of a rock. Capillary action, also known as capillarity, is a result of the intermolecular attraction within the liquid and solid materials.

**CAR policy** See Contract's All Risks policy.

**Case management conference (CMC)** A hearing, the first of one of which is usually held at an early stage of proceedings, at which the court reviews case preparation, gives directions and seeks agreements; see CPR Practice Direction 29 and s5 of the Technology and Construction Court (TCC) Guide.



Cantilever Bridge



Cantilevered beam



Cantilever Chair  
(Mies van der Rohe, 1927)

Figure C1 - Cantilever

## Case law update

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# Case law update

Our usual case round-up comes from two different sources. First, there is the Construction Industry Law Letter (CILL), edited by Karen Gidwani and Ted Lowery. CILL is published by Informa Professional. For further information on subscribing to the Construction Industry Law Letter, please contact Catherine Lauder by telephone on +44 (0) 20 7017 7974 or by email: [catherine.lauder@informa.com](mailto:catherine.lauder@informa.com). Second, there is our long-running monthly bulletin entitled Dispatch. This summarises the recent legal and other relevant developments. If you would like to look at recent editions, please go to [www.fenwickelliott.com](http://www.fenwickelliott.com). If you would like to receive a copy every month, please contact Jeremy Glover. We begin by setting out the most important adjudication cases as taken from Dispatch.

## Adjudication - Cases from Dispatch

### Adjudication: equitable set-off

#### *Beck Interiors Ltd v Classic Decorative Finishing Ltd*

CDF were engaged by Beck to carry out internal and external decoration works. Disputes arose and an adjudicator held that Beck was entitled to the sum of £36k plus VAT. CDF refused to pay arguing that the sum was not due as Beck owed CDF the sum of €60k relating to a project in Dublin. Beck issued enforcement proceedings. CDF said that they were entitled to set-off against the adjudicator's decision sums they claimed were due under a separate contract in Dublin. In the absence of a contractual right to set-off, did CDF have any equitable set-off rights? Mr Justice Coulson said the following:

- (i) The general principle is that it is rare for the court to permit the unsuccessful party in an adjudication to set-off against the sum awarded by the adjudicator some other separate claim. That would defeat the purpose of the Housing Grants Act;
- (ii) There are two possible exceptions; firstly where there were express set-off provisions in the contract, and secondly where the adjudicator did not order immediate payment, instead giving a declaration as to the proper operation of the contract;
- (iii) Neither of those exceptions applied here. There was no express contractual set-off provision in the subcontract and the adjudicator had told CDF to pay Beck "without further ado".

There remained the question as to whether CDF had any right of equitable set-off. Reference was made to the case of *Federal Commerce & Navigation Ltd v Molena Alpha Inc* [1978] 1 QB 927 where Lord Denning said that:

*"It is not every cross-claim which can be deducted. It is only cross-claims that arise out of the same transaction or are closely connected with it. It is only cross-claims which go directly to impeach the plaintiff's demands, that is, so closely connected with his demands that it would be manifestly unjust to allow him to enforce payment without taking into account the cross-claim."*

CDF's cross claim concerned a contract in Dublin and did not arise out of the same transaction that lay behind the adjudicator's decision. They were different contracts, entirely different projects, in two separate countries (and therefore two separate jurisdictions) and in two separate currencies. CDF did not therefore have any entitlement to equitable set-off.

### Adjudication: natural justice, legal advice

#### *Highlands and Islands Airports Ltd v Shetlands Islands Council*

This case arose out of the construction of an extension to runways at Sumburgh Airport. After the adjudicator's decision had been issued, SIC's solicitors discovered by chance that before reaching his decision the adjudicator had taken advice from senior counsel in relation to the

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*The general principle is that it is rare for the court to permit the unsuccessful party in an adjudication to set-off against the sum awarded by the adjudicator some other separate claim.*

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proper construction of clause 41.3 of the NEC Professional Services Contract. The adjudicator did not tell either of the parties that he had taken advice, nor did he tell the parties the terms of that advice, nor did he give the parties any opportunity to address him on the construction of clause 41.3. The adjudicator ordered SIC to pay some £2million. SIC refused to pay saying that there had been a breach of natural justice. The court heard evidence from the adjudicator, who had telephoned one counsel who was conflicted. The advice then received had been in the course of a short telephone call in which the adjudicator had asked whether senior counsel agreed with the view he had formed of what clause 41.3 of the contract meant. The call lasted no more than 2 or 3 minutes and it was a freebie, no fee was charged.

The adjudicator further said that he did nothing with counsel's response as he had already formed his own view of the meaning of the clause. In short he did not believe that he was seeking legal advice. In a previous adjudication, where he had required advice on an insurance matter, he had advised the parties of this and gave the parties the opportunity to comment on the identity of the proposed advisor and the advice itself. Indeed, in the adjudication in question, the adjudicator had instructed his own technical expert and again that report had been provided to the parties prior to the decision being given. SIC said that if an adjudicator is uncertain about a material issue and has taken advice from an independent source, he must tell the parties and give them an opportunity to make submissions. Neither of the parties knew that the adjudicator had a concern about the interpretation of the contract clause. If they had known this, they might well have wanted to make submissions about it.

To HIAC, the court should not be concerned with something which was at best a technical breach of natural justice. Here, SIC had the opportunity to respond to any issue (including the interpretation of clause 41.3) raised in the referral document. HIAC said that this was not something new, and the issue was not material to the determination of the dispute. Lord Menzies said that the rules of natural justice were designed to prevent the possibility of injustice. Here, the Judge considered that the confirmation sought by the adjudicator was indeed advice. It was given informally, it did not take long to impart, and no fee was to be paid for it, but nonetheless it was legal advice. It was legal advice which was sufficiently important to the adjudicator that when one counsel declined to speak to him because of a conflict of interest, he went on to telephone another to obtain advice on the point. It was also *"the foundation for any award in favour of HIAL for Future Remedial Works Costs."*

If the adjudicator had said that clause 41.3 was a matter which concerned him, or that he was intending to seek legal advice on this point, then either party might have made further submissions. You can only ignore non-material breaches of the principles of natural justice if there is a positive indication that the breach has not been material. If there is a significant doubt about the matter, it must be presumed that the breach is material. Therefore, Lord Menzies considered that the question was indeed of considerable potential importance, and was far from peripheral or irrelevant. It was central to the quantification of the largest part of the award made by the adjudicator. Therefore there was a breach and the decision was not enforced.

### Adjudication: forum shopping and alleged bias *Lanes Group plc v Galliford Try Infrastructure Ltd*

Galliford commenced adjudication and applied to the ICE to appoint an adjudicator. Mr Klein was appointed. However, Galliford's solicitors failed to take the next step, namely sending referral documents. As LJ Jackson characterised the position, the solicitors, honestly but mistakenly believing that Mr Klein was disqualified on grounds of bias, served a fresh notice of adjudication. They then applied to the ICE to appoint a new adjudicator. The ICE responded by appointing Mr Atkinson. Lanes' solicitors protested that he did not have jurisdiction, on the grounds that Mr Klein rather than Mr Atkinson was the only adjudicator appointed to resolve the dispute. During the adjudication, Mr Atkinson sent to the parties a document entitled "Preliminary Views and Findings of Fact". This set out his provisional conclusions. In due course both parties submitted their comments and submissions in relation to the Preliminary View. Mr Atkinson ultimately awarded Galliford £1.2million.

Lane challenged the validity of Mr Atkinson's appointment and the validity of his decision.

*It was given informally, it did not take long to impart, and no fee was to be paid for it, but nonetheless it was legal advice.*

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Did Mr Atkinson have jurisdiction as adjudicator? Lanes argued that s108 of the HGCRA and clause 18B of the sub-contract conditions permitted a party to refer a dispute to adjudication on one occasion only. If the party seeking adjudication did not follow through the reference, that was the end of the matter. The right to adjudication of the dispute notified in the notice was lost forever. Therefore, Galliford having allowed the adjudication before Mr Klein to lapse could not commence a new adjudication in respect of the same subject matter. LJ Jackson was initially attracted to this, noting that permitting a claimant to allow an adjudication to lapse because it disapproves of the appointed adjudicator and then to start a fresh adjudication before a different adjudicator was not appealing. However ultimately the Court of Appeal agreed with Galliford. There are occasions when an adjudication is not pursued further after the preliminary steps have been taken. There was no authority to suggest that this meant that the claimant would lose its right to adjudicate that dispute for ever. Second, the Blue Form subcontract, the ICE Adjudication Procedure and the Scheme recognise a right to restart an adjudication in a number of circumstances. It was therefore not right that a claimant's entitlement to adjudicate the dispute would be irretrievably lost. LJ Jackson said that:

***“Adjudication is a rough and ready process carried out at great speed. Vast masses of submissions and evidence have to be assimilated by the adjudicator in a short space of time. The adjudicator will fashion his procedure in whatever way enables him to discharge his onerous duties most swiftly, effectively and fairly.”***

*“Forum shopping is never attractive. My first view of this case was that Galliford could not be permitted simply to drop the first adjudication and then adjudicate before a different adjudicator whom it preferred.*

*Mr. Marrin's submissions have persuaded me, however, that Galliford's conduct was permissible under the contract and the second adjudicator did indeed have jurisdiction.”*

LJ Jackson then looked at the Preliminary View document and noted that the adjudicator used phrases such as “I find” and “I hold”. These statements were not intended to be decisions of the adjudicator but preliminary views and findings of fact preparatory to the decision. The preliminary views and findings are a step in making the decision and one is not bound by them. LJ Jackson thought that there was nothing objectionable in a judge setting out his provisional view at an early stage, so that the parties have an opportunity to correct any errors or to concentrate on matters which appear to be influencing the judge. There is, however, a clear distinction between (a) reaching a final decision prematurely and (b) reaching a provisional view which is disclosed for the assistance of the parties. Here, in LJ Jackson's view, the fair minded observer would have no difficulty in deciding that the Preliminary View was a provisional view, disclosed for the assistance of the parties, not a final determination reached before Mr Atkinson had considered all the submissions. The Judge said that he was reinforced in this by the fact that this was an adjudication, not an arbitration award or a judicial decision.

*“Adjudication is a rough and ready process carried out at great speed. Vast masses of submissions and evidence have to be assimilated by the adjudicator in a short space of time. The adjudicator will fashion his procedure in whatever way enables him to discharge his onerous duties most swiftly, effectively and fairly...An adjudication decision is not final. It is only binding until such time as the parties have concluded their litigation or their arbitration or their settlement negotiations or some other form of ADR.*

*Because adjudication has all these features, courts are reluctant to strike down adjudication decisions for breach of natural justice or on similar grounds, unless the complainant's case is clearly made out.”*

A comment parties would do well to bear in mind when considering challenging an adjudicator's decision.

### Adjudication: appointment of adjudicators

#### *Sprunt v London Borough of Camden*

This was an adjudication enforcement case where Mr Justice Akenhead had to consider whether or not there was a contract in writing as required by s107 of the old HGCRA. During the course of his judgment, the Judge made a couple of interesting comments

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about the extent and scope of the incorporation of the Scheme in circumstances where the underlying contract does not comply with s108 of the HGCRA and where a party says that it can choose the adjudicator. Clause 25 of the contract indicated that:

*25.4 The Council shall be the specified nominating body for the purposes of paragraphs 2(1)(b) and 6(1)(b) of Part 1;*

That clause went on at paragraph 25.11 to list a number of circumstances where if any decision of the adjudicator required either party to make payment to the other, then such decision would be suspended. Camden conceded that the clause offended against the requirement that adjudication decisions are binding until they are resolved by legal or arbitration proceedings. The Scottish case of *Profile Projects v Elmwood* had suggested that there was no reason why only part of the Scheme could not be implied into the contract in question in respect of any parts of that contract which that were not compliant with section 108. Mr. Justice Akenhead confirmed that this did not apply in England & Wales. He thought that the wording of s108(5) was "reasonably clear": "If the contract does not comply with the requirements of subsections (1) to (4), the adjudication provisions of the Scheme for Construction Contracts apply." He added that:

*"...if there is in the contract adjudication provisions at least one material non-compliance, they all go."*

***"...if there is in the contract adjudication provisions at least one material non-compliance, they all go."***

Then there was the question of the nomination of the adjudicator. Sprunt approached the RICS. Camden argued that it was the nominating body. The Judge noted that the concession that clause 25.11 was contrary to s108(3) of the HGCRA, meant that all the adjudication provisions of the Scheme applied. However he then went on to make a further, in his words, "stronger point", namely that: "it is inherently unsound and contrary to the policy of the HGCRA for the contract to specify that one side should nominate the adjudicator. Section 108(2)(e) imposes a statutory requirement that the contract should impose a duty on the adjudicator to act impartially. Impartiality in an adjudicator, or indeed an arbitrator or judge, is judged in two ways, the first being by reference to actual partiality or bias and the other by reference to ostensible or apparent partiality or bias."

The Judge stressed that he was not suggesting any actual bias on the part of Camden, but he did note that it would be difficult to dispel the real possibility that Camden had appointed what it thought was a "horse for the course" and someone who was or might be sympathetic to Camden. The fact that Camden were a party to the construction contract in question meant that it lacked the necessary quality of independence in the nomination of an adjudicator. Here, adjudication was different to arbitration as there is only a limited time in which a party to adjudication can determine if an adjudicator nominated by the other party is or might be considered potentially, actually or ostensibly partial or biased. The Judge concluded that:

*"Essentially, what Camden would have is not a judge in its own cause but the right to nominate a judge in its own cause and that strikes against the policy of the act of having actually and ostensibly impartial adjudicators."*

### Adjudication: was there a dispute?

#### ***Working Environments Ltd v Greencoat Construction Ltd***

Greencoat engaged WE to carry out the mechanical services installation as part of substantial fitting out works at existing office accommodation. Under the sub-contract provision was made for WE to apply for payment on the second to last Friday of each month and for Greencoat to issue a payment certificate within one week thereafter. The final date for payment was to be 45 days after receipt of an invoice by WE. WE submitted Application No 10 for payment for a net sum of £488k. This included breakdowns as to how that figure was reached. Greencoat certified that a net sum of only £16.6k was due, again providing breakdowns against various heads of work done, variations and withheld items. Under the sub-contract, payment was due by 14 January 2012. On 8 December 2011, WE's consultants confirmed that they did not accept Greencoat's assessment. They started adjudication proceedings 6 days later.

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*It would be illogical to say that there cannot be a dispute about an interim valuation of work unless, until and after the valuation falls due for payment. The fact is that here there was a dispute about the interim valuation and that dispute was referable to adjudication.*

Greencoat said that the adjudicator effectively had no jurisdiction on the basis that no dispute or no material dispute had crystallised because the date for payment had not yet accrued, and because relief for payment was sought which the adjudicator could not award because the obligation to pay had not arisen. The adjudicator replied saying "I also doubt that the fact that payment is not yet due is a good point". The Judge agreed saying that it was clear that there was a dispute as to whether £488k or some other sum was due. The Judge noted that it would be illogical to say that there cannot be a dispute about an interim valuation of work unless, until and after the valuation falls due for payment. The fact is that here there was a dispute about the interim valuation and that dispute was referable to adjudication. Any dispute would cover the items put forward for withholding, as effectively Greencoat was arguing that the items and quantum then claimed could and should be deducted, whilst WE was arguing that they could and should not be deducted.

There were however two items totalling approximately £25k which were not part of or within the confines of the dispute as they had not been mentioned before they emerged 22 days into the adjudication process. The Judge was of the view that, he was able to sever that part of the decision where the adjudicator did not have jurisdiction and reduce the total sum due accordingly. To act in this way was entirely consistent with the principles set out in the *Cantillon v Urvasco* decision where Mr Justice Akenhead himself had noted that:

*(c) If the decision properly addresses more than one dispute or difference, a successful jurisdictional challenge on that part of the decision which deals with one such dispute or difference will not undermine the validity and enforceability of that part of the decision which deals with the other(s).*

*(d) The same in logic must apply to the case where there is a non-compliance with the rules of natural justice which only affects the disposal of one dispute or difference.*

### Other cases

#### Construction Industry Law Letter

### Preservation of handover documents

#### *Alstom Power Ltd v Somi Impianti S.r.l.*

Technology and Construction Court: before Mr Justice Akenhead: judgment delivered 21 November 2011

##### **The facts**

Alstom was appointed by RWE npower plc as the main contractor to engineer, procure and construct a substantial power plant in Pembrokeshire. Alstom engaged Somi to carry out mechanical and piping erection and plant piping and mechanical erection works. The Sub-Contract conditions included at clause 54.1 a provision prohibiting the removal from site of the Sub-contractor's Equipment and materials, the former being widely defined to encompass "...all appliances and things of whatsoever nature, other than Temporary Works, required for the execution and completion of the Works..." Clause 54.2 provided that whilst on site the Sub-contractor's Equipment would be deemed to be the property of Alstom and clause 54.14 required the delivery to Alstom of all such equipment if for any reason Somi's employment was terminated prior to completion of the Sub-contract works.

Somi's works were delayed. Alstom alleged that Somi was financially unable to proceed with the project and had deliberately failed to comply with health and safety obligations. Alstom terminated Somi's employment albeit that this termination was subsequently challenged by Somi in adjudication. During the run-up to handover Alstom was required to provide RWE with a substantial volume of documentation including what were described as 'Turnover Packages' usually referred to as 'TOPs'. These TOPs included information verifying the proper design, manufacture and fabrication of various units

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comprising the Sub-contract works together with other critical data relevant to each unit. Prior to 15 August 2011 Somi had brought to site the TOPs for most of the units. However, following termination around a quarter of the TOPs were removed from site by Somi and taken back to Italy. Alstom issued an application for various interim injunctions concerning the preservation and return of the TOPs, contending that damages would not be an adequate remedy where the TOPs were required so that Alstom could complete handover to RWE by April 2012 and where some of the constituent documents within the TOPs could not be readily recreated.

### *Issues and findings*

Was Alstom entitled to an interim injunction requiring Somi to return the TOPs?

Yes. Damages would not be an adequate remedy as it was likely that Somi would not be able to meet a monetary judgment, particularly bearing in mind, the substantial additional costs that Alstom might incur if the TOPs were not handed over.

### *Commentary*

The Judge clearly recognised the importance of the TOPs documents to Alstom when it came to meeting their contractual obligations to their employer. The Judge also accepted Alstom's evidence that damages would not be an adequate remedy where the financial position of Somi made it unlikely that damages would be recovered and where some of the documents within the TOPs could not have been obtained other than through Somi.

In major projects, particularly in the power and processing engineering sector, there will be a great deal of information to be handed over to the employer on completion and often, as in this case, the necessary certification for plant and equipment packages may only be available through the sub-contractor installers. In these circumstances it may be tempting for the subcontractor to seek to gain a commercial advantage by withholding this important information. In this case, the Judge found that one of the main reasons why Somi was holding onto the TOPs was as a bargaining chip in negotiations and this finding contributed to his conclusion that damages would not be an adequate remedy.

Each case will of course turn upon its own facts and it is significant that Somi's Sub-contract contained express provisions that vested title in the TOPs in Alstom where the TOPs fell within the wide definition of Sub-contractor's Equipment set out in the Sub-contract. The position will not be as clear where there is no vesting clause in the contract and an interim injunction is unlikely to be obtained if for example the Sub-contractor has managed to include a clause that provides that documents will not be handed over until full payment has been received.

## Non-statutory limitation clause – time bars

### *Inframatrix Investments Ltd v Dean Construction Ltd*

Court of Appeal: before Lord Justice Stanley Burnton, Lord Justice Aikens and Lord Justice Elias: judgment delivered 3 February 2012

### *The facts*

DCL was engaged by Inframatrix to perform specialist roofing and cladding works ('the Services') at a new camera factory. The original draft of the contract proposed a 12-year limitation period for claims against DCL but following an amendment proposed by DCL, the executed version included a provision at clause 17.4 that no proceedings could be brought against DCL after (a) the expiry of one year from the date of Practical Completion of the Services or (b) where such date did not occur, the expiry of 1 year from the date on which DCL last performed, "... Services in relation to the Project." The Contract included a definition of Practical Completion of the Project but not of the Services.

DCL carried out its works during November and December 2008. Following a site inspection on 8 January 2009 Inframatrix's engineer notified DCL of a number of defects. DCL returned to site to attend to these defects and on 9 February 2009 notified

*It may be tempting for the subcontractor to seek to gain a commercial advantage by withholding important information as a bargaining chip in negotiations.*

*But this finding contributed to the conclusion that damages would not be an adequate remedy.*

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*When given their natural meaning the words in the clause could be readily understood and the implied additional wording was neither necessary nor justified.*

Inframatrix that the building was complete. No certificate of Practical Completion of the Services was ever issued. DCL demanded payment of outstanding sums due under the Contract but Inframatrix alleged poor workmanship and requested that DCL remedy defects as a pre-condition to payment. DCL's position was that having attended to the matters notified during January 2009, its works had been completed. DCL also alleged that the defective items were the result of damage caused by other contractors.

Inframatrix issued a letter of claim under the Pre-Action Protocol. In its letter of response, DCL offered on a without prejudice basis to meet on site in order to identify any required remedial work. Inframatrix accepted this proposal and the meeting took place. Following the meeting DCL provided Inframatrix with a report on a without prejudice basis and offered to return to site to carry out further investigation work and remedial work if necessary. Inframatrix did not accept this offer and did not allow DCL to return to site.

Inframatrix issued proceedings claiming damages for breach of the Contract. In its Defence DCL contended that the proceedings were time barred by the provisions of clause 17.4 of the Contract on the basis that it had last carried out Services in February 2009. DCL therefore applied to strike out the damages claim. In response Inframatrix contended that practical completion of the Services had not been achieved and argued that clause 17.4(b) only applied where practical completion was never going to be achieved, for example, if the Project had been abandoned. Inframatrix further submitted that the meeting on site amounted to performance of Services thus triggering a fresh limitation period under clause 17.4(b).

At first instance the Judge rejected Inframatrix's arguments observing that the latter's suggested interpretation of clause 17.4(b) flouted business common sense. He held that DCL's participation in the meeting on site and subsequent production of the report on a without prejudice basis did not constitute the carrying out of Services under the Contract. In its appeal Inframatrix additionally argued that additional wording ought to be implied into clause 17.4(b) to support its interpretation of the proper meaning of this provision and reflect what the parties must have intended. Inframatrix argued that it should be assumed that DCL's return to site amounted to the provision of Services unless DCL expressly stated otherwise. It was insufficient that DCL reserved its position on a without prejudice basis. Finally, Inframatrix sought to rely upon the principle established in *Alghussein Establishment v Eton College*, arguing that DCL should not be entitled to a contractual construction that would enable it to benefit from its own wrong.

### **Issues and findings**

Should additional wording be implied into clause 17.4(b) to make the clause applicable only in situations in which practical completion was never going to be achieved?

No. That was not the meaning intended by the parties. When given their natural meaning the words in the clause could be readily understood and the implied additional wording was neither necessary nor justified.

Did attending the meeting on site and subsequent production of a report by DCL amount to carrying out Services under the Contract?

No. Where these activities were carried out on a without prejudice basis they could not amount to contractual performance.

Did the principle in *Alghussein* apply?

No. The context of this dispute was very different where the limitation clause was intended to apply only where there was an allegation of breach of contract against DCL.

### **Commentary**

In this case the Court of Appeal firmly endorsed the decision of the lower court. The Judge at first instance had concluded that Inframatrix's proposed interpretation of clause 17.4(b) flouted business common sense and the Court of Appeal came to the same conclusion,

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noting that if the implied words contended for by Inframatrix were to be added to clause 17.4(b) this would have the effect of allowing Inframatrix complete control over the date upon which time began to run. Lord Justice Elias observed that there was no inference that this was the intention of the parties and that if this had been intended then clear words should have been included to reflect this meaning.

The Court of Appeal re-stated the principle that the words used in written instruments should be given their natural meaning and that where plain words were used that could be readily understood, there was no need to imply additional wording to produce a contrary construction.

Albeit that DCL had returned to the site and provided a report setting out proposed further works, the Court of Appeal had little hesitation in finding that what was described as the “without prejudice wrapper” prevented Inframatrix from asserting that DCL’s activities were being undertaken pursuant to the Contract. DCL had carried out these activities on a without prejudice basis specifically in order to preserve its position. Lord Justice Stanley Burnton noted that where activities had been carried out for the purposes of negotiating a possible settlement they could not amount to contractual services.

Finally, the Court rejected the argument that the principle in *Alghussein* applied. Where the limitation clause in the Contract was only intended to apply in circumstances where a breach of contract had been alleged against DCL then the limitation clause would be rendered ineffective if Inframatrix were to be allowed to rely upon that breach to apply the *Alghussein* principle.

The Court of Appeal thereby upheld a contractual limitation period of one year. This may come as something of a surprise to those of us who are used to six-year and twelve-year limitation periods but this case demonstrates that if expressed sufficiently clearly in the contract, a shorter limitation period will be enforceable.

*The Court of Appeal upheld a contractual limitation period of one year, which may come as something of a surprise to those who are used to six-year and twelve-year.*

## Proper interpretation – latent defects – patent defects

### *Point West London Ltd v Mivan Ltd*

Technology and Construction Court: before Mr Justice Ramsey: judgment delivered 10 May 2012

#### ***The facts***

During the 1990s Point West began developing a site at 116 Cromwell Road in west London. On 22 August 2000 Point West engaged Mivan as main contractor for Phase 4 of the developments works comprising the construction of 48 apartments. The contract incorporated the JCT Standard Form of Building Contract with Contractor’s Design (1998 Edition). Practical completion was certified but no certificate of making good defects was issued. On 16 July 2002 the final account valuation for Mivan’s contract works was agreed.

During July 2002 Flat 1601 was sold leasehold to a Trust. At the time of the sale, Point West was aware of problems with the curtain walling system that had caused water ingress at Flat 1601 and some £25,000 was held back from the purchase price by way of retention. Subsequently defects were also discovered in the flat’s heating and cooling system. During the period 2002–2007 Mivan carried out further works at the site. These works included snagging of their own works and ‘basebuild’ snagging of works by others. During the same period various investigations were carried out by Mivan and Point West but none of the consequential remedial works managed to achieve permanent rectification of the water ingress and heating problems in Flat 1601 and the Trust began to withhold service charge payments and other sums due under the lease.

Over 15-18 October 2007 three letters passed between the parties which formed the settlement agreement under which Mivan were to receive a further payment of £50,000 including VAT. The first letter was sent by Mivan to Point West on 15 October 2007 and confirmed ‘*the agreement reached regarding Mivan’s Final Account in respect of all Works carried out, and any corresponding outstanding matters. The agreement comprises a further*

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*payment of £50,000 (including VAT), representing the final assessment of monies due or to become due thus achieving full and final settlement in respect of the above works, together with any outstanding matters. We would confirm that this final agreement concludes Mivan's responsibilities and obligations in respect of their works at the above project...'*

Point West responded on the 18 October 2007 confirming that, 'the contents of your letter are accepted subject to you being prepared to assist [Point West] in the legal aspects of the case on Flat 1601. This may involve some time on the part of Mivan along with the production of necessary documents but I am not looking to you to do any further remedial works.' Mivan replied the same day to confirm their reasonable assistance in connection with the impending legal proceedings against the Trust. At the time of the Settlement Agreement both Point West and Mivan were aware that (a) there were persistent, known and unresolved defects in the curtain walling system; and (b) there were defects in the heating and cooling system which were of an unknown scope and extent.

***The terms of the Settlement Agreement released Mivan from any liability for all defects that were patent at the time the agreement was entered into and the defects in the curtain walling and heating and cooling system were evidently patent as at 18 October 2007.***

Point West commenced proceedings against the Trust for arrears of service charge and other sums due under the lease. The Trust said that the curtain walling and the ventilation system suffered from widespread defects necessitating complete replacement. The County Court awarded damages to the Trust. Point West brought a claim against Mivan saying that: (i) the Settlement Agreement was a financial settlement in relation only to the further works carried out by Mivan after the final account agreement; (ii) the defects in the curtain walling and the heating and cooling system that were known about up to October 2007 were commonly regarded as minor workmanship failings and not the fundamental defects alleged by the Trust in the County Court, and (iii) these 'Fundamental Latent Defects' were not known about in October 2007 and were therefore not covered by the Settlement Agreement.

In response, Mivan argued that the Settlement Agreement precluded Point West from seeking damages for specific performance in relation to (a) the defects forming the subject matter of the County Court proceedings; and (b) any other defects in the development which were patent as at 18 October 2007. Point West argued that during 2007 there was no suggestion of a potential claim against Mivan for the defects. The Settlement Agreement only resolved any potential disputes over the monies due to Mivan for works carried out post final account agreement. If there had been an intention to fully discharge Mivan's accrued liabilities then this should have been spelled out.

### ***Issues and findings***

Did the Settlement Agreement encompass Mivan's liability in respect of the curtain walling and heating and cooling system defects?

Yes. The terms of the Settlement Agreement released Mivan from any liability for all defects that were patent at the time and the defects in the curtain walling and heating and cooling system were evidently patent as at 18 October 2007.

### ***Commentary***

There are no special rules governing the interpretation of settlement agreements and the Court will therefore apply the same principles used when construing a contract. However, here the Judge also noted that when applying these principles, a Court should be slow to infer that either party intended to surrender any rights and claims of which it was unaware or could not have been aware of at the time it entered into the settlement agreement.

Point West's principal submission was that as at 18 October 2007, the parties were unaware of the serious nature of the defects in the curtain walling and heating and cooling systems and absent specific wording in the Settlement Agreement, could not therefore be taken to have intended compromising Mivan's potentially extensive liability for these defects. Point West's position was that in circumstances where in October 2007 both sides considered that the defects were insignificant, the Settlement Agreement could not be taken to have settled a dispute that neither party was contemplating at that time.

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Applying the usual principles of construction, the Judge concluded that the Settlement Agreement did encompass Mivan's liabilities in respect of the evidently patent defects within the curtain walling and ventilation system in the Flat. In particular the Judge noted the use of the words, 'all Works' and 'all outstanding matters' in the Settlement Agreement which suggested that the agreement was intended to bring to an end Mivan's obligations in respect of all of the Phase 4 works. This included any and all outstanding matters and defects that were patent at the time. The extent of the parties' appreciation of the scale of these defects at the time that the Settlement Agreement was entered into was immaterial.

From the point of view of business common sense, the Judge concluded that where the Settlement Agreement included a statement by Point West that it was not expecting Mivan to carry out any more remedial works, it would be impossible to interpret the agreement as meaning that this statement was to be subject to Point West's continuing entitlement to claim any costs incurred in having remedial works carried out by others.

The words of any settlement agreement must be clear and unambiguous so that the extent and scope of the compromise is clearly identifiable. Parties should ensure that the terms as drafted accurately reflect their intentions. Ambiguity and uncertainty can lead to costly disputes. Here, the Judge questioned Point West's commercial decision to focus on the proceedings against the Trust but further noted the general principle that the Courts will not remedy any lacunae in the parties' bargain or construe an agreement so as to improve or make a contract which the parties did not make for themselves.

### Failure to effectively manage electronic disclosure – wasted costs orders

#### *West African Gas Pipeline Company Ltd ("WAPCO") v Willbros Global Holdings Inc ("WGH")*

Technology and Construction Court: before Mr Justice Ramsey; judgment delivered 27 February 2012

##### ***The facts***

WAPCo engaged WGH as an EPC contractor for the construction of a 421 mile gas-pipeline between Nigeria, Benin, Togo and Ghana. Disputes arose and WAPCo commenced proceedings against WGH in the TCC seeking recovery under the guarantee of US\$273,748,113 and additional completion costs. There was extensive correspondence between the parties' solicitors concerning errors and omissions in WAPCo's disclosure. WAPCo's solicitors referred to problems with the de-duplication process carried out by WAPCo's external litigation support provider that had led to a significant proportion of duplicate documents being included in the disclosure. WAPCo also stated that they had instructed another litigation support company based in India to carry out a further review of the documents. This review had resulted in a large number of documents being reclassified as discloseable. Further, redactions had been incorrectly applied, something that was blamed upon the failure to de-duplicate documents properly. WGH claimed the wasted costs said to have been incurred in dealing with WAPCo's inadequate disclosure.

Whilst accepting that there had been failures in its disclosure, WAPCo submitted that these had to be viewed in the light of what was a complex and difficult international dispute and that it was inappropriate to make wasted costs order until the relevance of material disclosed late could be established at trial.

##### ***Issues and findings***

Was WGH entitled to a wasted costs order in respect of the additional costs incurred in dealing with WAPCo's disclosure?

Yes. As a result of WAPCo's failure to gather the documents together and carry out a proper review, WGH's disclosure exercise had been prolonged and disrupted and increased costs had inevitably been incurred.

*The Court should be slow to infer that either party to a settlement agreement intended to surrender any rights and claims of which it was unaware of or could not have been aware of at the time it entered into the agreement.*

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### Commentary

Construction projects ordinarily generate large amounts of documents and the volumes will usually increase in proportion to the size and value of the works being undertaken. On big projects, both the main contractor and the employer will usually maintain bespoke document management systems in which the documents generated are organised in electronic libraries, indexed and cross referenced. The basic obligation when giving disclosure under CPR Part 31 remains to gather in and identify all documents that may potentially be relevant and strip out those that are irrelevant, duplicates or privileged. It is therefore important to establish at an early stage the extent and location of the potentially relevant documents both in hard copy and in electronic copy. The significance of electronic data is recognized in the CPR: Rule 31.4 establishes a wide definition of “document”, i.e. anything in which information of any description is recorded.

*As a result of WAPCo’s failure to gather the documents together and carry out a proper review, WGH’s disclosure exercise had been prolonged and disrupted and increased costs had inevitably been incurred.*

Practice Direction 31A includes an equally wide definition of “Electronic Document” i.e. any document held in electronic form, to include emails, word processed material and databases, previous iterations of final version documents, documents that have been deleted but which can be recovered, documents stored on portable devices and servers, metadata and embedded information not otherwise visible on screen or in the hard copy. In accordance with Rule 31.7, searches for documents need to be reasonable and proportionate and the Practice Direction provides that for Electronic Documents, the primary source for disclosure will be data that is normally reasonably accessible. In practice this still means that where an order for standard disclosure is made, the parties’ disclosure obligations in relation to Electronic Documents will be onerous and extensive, even on a project of modest size. Practice Direction 31A contains detailed provisions for the disclosure of Electronic Documents (‘e-disclosure’) and opens with the general principles that Electronic Documents should be managed efficiently in order to minimise the costs incurred and that technology should be used in order to ensure that document management activities are undertaken efficiently and effectively.

In order to improve the efficiency of the process when giving e-disclosure it is usual practice to de-duplicate multiple electronic copies (for example by removing preceding communications from lengthy email chains) and establish a protocol for redacting irrelevant or privileged text. Over the last few years parties to large disputes have begun to arrange for e-disclosure to be managed by legal support services companies that offer software and personnel to carry out the necessary reviews, including de-duplication and redaction, of electronic documents.

This case illustrates some of the problems that may be encountered when trying to manage vast amounts of electronic paperwork that may, in an international project, be located in various parts of the world. The Judge agreed that WAPCo had badly managed its disclosure and identified three major failings by WAPCo that were sufficient to justify an order for wasted costs in favour of WGH, i.e. that WAPCo had failed to de-duplicate, that WAPCo had applied inconsistent redactions and that WAPCo had generally failed to properly gather in the material documents. It seems clear that WAPCo’s first sweep for Electronic Documents had not been anywhere near as comprehensive as it should have been and the Judge referred to WAPCo’s general failure to “harvest” the documents. The initial failures to disclose clearly material emails exemplified WAPCo’s general failure to properly organise its disclosure. WGH’s claim for wasted costs was spread across its lawyers, consultants, legal support team and experts. The Judge expressed doubt that a proper allocation of the costs that were recoverable was possible on the basis of the information presented by WGH. He concluded that costs could not be dealt with on summary assessment and ordered an interim payment of £135,000. It seems likely that disclosure costs will increase as the parties and their lawyers will err on the side of caution and become more assiduous when giving e-disclosure in order to guard against the risk of applications for wasted costs orders founded upon this judgment.

However, TCC Judges can be expected to encourage the parties to try to agree cost-saving alternatives to giving standard disclosure of Electronic Documents and the Court will actively case manage the e-disclosure process if the parties show any signs of dithering.

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Welcome to the July edition of *Insight*, Fenwick Elliott's newsletter which provides practical information on topical issues affecting the building, engineering and energy sectors.

**In this issue find out about Project Bank Accounts.**

# Insight

## Project Bank Accounts - the way forward?

Since their launch five years ago, Project Bank Accounts have been used on public sector contracts worth £2.5bn. In line with the Government Construction Strategy, the Government has confirmed Project Bank Accounts will be used on public sector projects "unless there are compelling reasons not to do so". Project Bank Accounts are therefore quickly becoming standard in public sector procurement and their use might become just as widespread in private sector procurement in the not too distant future.

This thirteenth issue of *Insight* considers (i) how Project Bank Accounts work in practice; (ii) their advantages and disadvantages; and (iii) practical advice for newcomers to Project Bank Accounts.

### What is a Project Bank Account?

Project Bank Accounts (PBAs) are ring-fenced bank accounts whose sole purpose is to act as a channel for payment on construction projects to ensure that contractors, key subcontractors and key members of the supply chain are paid on the contractually agreed dates.

The employer maintains adequate funds in the account to cover work in progress and other project commitments. Payments are made directly from the account to the contractor, key subcontractors and key suppliers in accordance with the payment arrangements agreed by those members of the project team who are party to the PBA.

### How does a PBA work in practice?

In the usual course of events, the PBA is set up by the employer either in the employer's own name (in which case the employer might give the contractor's representatives authority to act under a bank mandate) or in the employer's and contractor's joint names on trust for the key subcontractors and key members of the supply chain. If the latter approach is taken, the key subcontractors and key members of the supply chain would be party to the trust deed.

PBAs differ from the usual payment mechanism in that instead of paying the certified sum to the contractor, the employer funds the PBA one or two months in advance (and therefore in advance of the progress of the works). To ensure the balance remains positive, the employer will usually have a detailed and frequently updated payment schedule which sets out the envisaged construction costs in each month of the project.

Each month, the contractor, subcontractors and consultants submit their payment applications in the usual way. Interim certificates are issued and agreement is reached as to the entitlement of the project team to a proportion of the sum certified. The account holders then instruct the bank to remit payment of the certified sum and payment from the PBA

discharges the sums due under the main and subcontracts.

If the employer's payment needs to be reduced, due to the contractor's default for example, then the contractor may be required to make a top-up payment into the account so that subcontractors and suppliers can be paid. Equally, the employer (or if there is a shortfall or the employer fails to make payment, the contractor) may be required to ensure the balance remains at an agreed minimum level.

Each member of the PBA has direct signing rights over the PBA and as soon as a payment has been certified, each party can withdraw the certified sum to which it is entitled instead of having to wait to receive payment from the employer or from those higher up the contractual chain.

### Advantages

The advantages that accrue from the use of PBAs are ultimately financial and this is of particular note in the current climate.

#### *Security of payment*

Provided the PBA is properly set up, the principal advantage of a PBA as far as contractors and the rest of the project team are concerned is that in the event of an insolvency in the contractual chain, payments can still be made to members of the project team.

The developer also benefits since the risk of an employer having to pay suppliers and subcontractors for the same work twice in circumstances where the contractor fails to remit payment and then becomes insolvent falls away.

#### *Speed of payment*

PBAs should speed up payment and reduce payment abuse, particularly for those lower down the supply chain for whom late payment can have a significant impact against what are often very tight margins. The reason for this is that payment does not have to flow down the contractual chain; instead, those members of the project team who are party to the PBA are paid directly from the PBA.



## Insight

### *Cash flow management*

Management of cash flow is transparent under a PBA in that the contractor and supply chain benefit from having the certainty that money has been paid into the PBA in advance of the date on which payment falls due.

One of those to benefit from PBAs is the smaller contractor further down the supply chain who has to tolerate compounded payment periods. Paying parties at the lower end of the contractual chain often find themselves having to gradually extend their own payment periods as onward payment is only made upon receipt of funds from those higher up the chain. This makes things very difficult for smaller subcontractors and suppliers who effectively have to trade on credit.

### *Cost savings*

The Government estimates that if they are properly implemented across the board, PBAs can deliver up to 2.5% in savings in the cost of construction projects.

These cost savings arise by virtue of the fact that (i) supply chain members do not have to chase for payment, thus reducing administration charges, and (ii) the need to finance lengthy credit periods reflective of the long payment chains from employer to contractor, from contractor to subcontractor and from subcontractor to supplier, is eliminated.

### **Disadvantages**

Fortunately for contractors, the disadvantages of PBAs only affect employers and funders.

### *Set-up costs*

PBAs can cost money to establish and run, and the negotiations that lead to the setting up of a PBA can be lengthy. Unless the groundwork is put in in the early stages of a project, the administrative burdens of a PBA as well as the training costs for an unfamiliar project team may

be disproportionately high. PBAs are therefore most suitable for larger-scale projects or related schemes of work.

### *Loss of control from employer / funder's perspective*

A PBA can also reduce the control a bank or employer has over a project: if money is tied up in a PBA it may not be able to be used for other purposes.

In terms of the payment mechanism, if an employer needs to make a deduction for defective work, it will need to ensure that the PBA arrangements allow it to act upon such a deduction. If a deduction is justified by virtue of a main contractor error, then the main contractor may need to pay more money into the PBA to enable subcontractors and suppliers to be paid.

### *Payment disputes will remain*

Although the use of a PBA can provide greater certainty around payment, it does not guarantee that correct payments will be made, nor will it eliminate payment disputes. The usual procedures for making payment still need to be adhered to, queries about a contractor's account still need to be answered and the employer can still withhold payment or set off sums that might otherwise be due (provided of course that the PBA arrangements allow the employer to do so).

### **Practical advice for newcomers to Project Bank Accounts**

To receive the above benefits that PBAs can bring, in particular security for payment from which the other benefits then flow, the PBA must create a trust in favour of the contractor in order to be effective.

If a trust exists and the employer becomes insolvent, it is generally understood that the funds in a properly constituted PBA will not fall to be included with the employer's other assets and they should therefore be protected from the hands of creditors. If there is no trust in favour of the contractor, in the event of insolvency, the contractor will probably rank as an unsecured creditor and will receive little if anything by way of a return on its debt.

In practice, identifying whether a trust exists in relation to the balance of a PBA of an insolvent company can be difficult. If, for example, the insolvent company mixes its own funds with trust funds, it can cause the trust to fail. It is therefore of paramount importance that the trust mechanism is approved by a trust specialist to ensure it will be effective upon any insolvency.

Also of importance is to double check that the terms of the PBA documentation dovetail with the payment provisions in the building contract. The provisions in the building contract must also make clear how the PBA is to be set up and funded, and how payments are to be made following on from the certification process. If this is not the case, there is a risk the payment mechanism may break down, in which case the speed and security of payment, cash flow management and cost-savings benefits mentioned above may fall away.

### **Conclusion**

The advantages of PBAs almost certainly outweigh any disadvantages, and whilst PBAs are heavily favoured by the majority of industry commentators, their use is not yet commonplace. This lack of use is most likely reflective of the reluctance of members of the construction industry to move into new territory at a time where market conditions are uncertain and Building Information Modelling is also on the horizon.

The widespread use of PBAs may well revolutionise the way the construction supply chain gets paid and it will therefore be interesting to follow the progress of PBAs as the construction sector begins to recover.

Should you wish to receive further information in relation to this briefing note or the source material referred to, then please contact Lisa Kingston. [lkingston@fenwickelliott.com](mailto:lkingston@fenwickelliott.com). Tel +44 (0) 207 421 1986

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