

Annual Review of English Construction Law Developments

An international perspective

August 2022

Contents

3	Introduction
4	Force majeure and frustration claims arising from the Covid-19 pandemic: a comparative survey
12	Limitation of liability in construction contracts: the relevance of intentional or repudiatory breaches
16	Parent company guarantees as on-demand bonds: a softening of the English law approach
22	Challenging bond calls on international projects: English courts vs Emergency Arbitrators
26	Liquidated damages and termination: orthodoxy restored
30	Liquidated damages and partial taking-over
34	"No oral modification" clauses: an international divide
40	Negotiating agreements and endeavours clauses
46	Deemed design liability
50	Cross-border enforcement of statutory adjudication decisions
54	International English Law Construction Contracts



I simply consider this to be 'mandatory literature' for anyone interested in construction law.

General Counsel, Global Energy Company

CMS Law-Now™

Your free online legal information service.

A subscription service for legal articles on a variety of topics delivered by email.

www.cms-lawnow.com

Introduction

Welcome to the 2022 edition of our internationally focused *Annual Review of English Construction Law Developments*, covering developments from across the globe relevant to international projects governed by English law.

We open this year's Review with a comparative survey of force majeure and frustration claims across four common law jurisdictions. The Covid-19 pandemic has seen an increase in such claims on construction projects and, whether founded in contract or general law, significant differences exist as to how these claims are approached in the jurisdictions surveyed.

The difficult economic circumstances precipitated by the pandemic has continued to see English law developments in relation to on-demand bonds. Of particular note is a broadening of approach by the English Court of Appeal as to when parent company guarantees will be held to be truly on-demand.

Contractual allocations of risk also provide a significant theme for this year's Review. We report on a case from Singapore which departs from the UK approach to "no oral modification" clauses with significant implications for construction projects. The English courts have also considered the approach to limitation of liability clauses in circumstances of intentional or repudiatory breach. We also report on two Scottish cases dealing with "deemed design liability" clauses, showing that their effectiveness depends very much on the circumstances.

Liquidated damages provisions have been before the English courts with increased frequency of late. We report on a UK Supreme Court decision which has settled the question of how such clauses operate in

termination scenarios. A different case has considered the effect of partial possession rights on the enforceability of liquidated damages provisions which do not allow for downward adjustments.

We have also revisited the topic of endeavours clauses and negotiating agreements in light of what appears to be the first English court decision to enforce an agreement to use reasonable endeavours to conclude a further agreement. English law has long held an antipathy toward such agreements and this decision may allow some limited recognition to be given to them in the future.

Another novel issue covered in this year's Review is the enforcement of adjudication decisions given pursuant to local law where the construction contract is governed by a foreign law and subject to the jurisdiction of foreign courts. An English court has decided in favour of local enforcement, but the result in other jurisdictions may depend on policy considerations and the terms of any relevant treaties.

As always, we hope you find this publication useful and we welcome any comments or feedback you may have. Should you wish to receive more frequent updates throughout the coming year, or for briefer summaries of developments earlier this year, please sign up for our Law-Now service at www.law-now.com and select "Construction" as your chosen area of law.



David Parton

Partner, Head of Construction
T +44 20 7524 6873
E david.parton@cms-cmno.com



Steven Williams

Partner, Co-Head of Infrastructure
Construction and Energy (ICE) Disputes
T +44 20 7524 6713
E steven.williams@cms-cmno.com



Adrian Bell

Partner, Co-Head of Infrastructure
Construction and Energy (ICE) Disputes
T +44 20 7367 3558
E adrian.bell@cms-cmno.com

Force majeure and frustration claims arising from the Covid-19 pandemic: a comparative survey

The Covid-19 pandemic has caused major disruption to many industries around the world, not least to construction projects. This disruption has given rise to widespread claims for relief from contractual obligations impacted by the pandemic, both under general law principles and express contractual provisions. We set out below a short comparative survey across England, Singapore, the United States and Australia covering the differing approaches to these claims as well as some recent examples arising in the wake of the pandemic.



England

English law does not have any independent doctrine of “force majeure” as a legal principal. In its place it has the doctrine of frustration. Frustration under English law can be viewed from a number of perspectives:

- **Supervening Illegality.** The English Courts will not enforce performance of an English law governed contract that requires a party to perform actions which have become illegal under the law of the country in which those actions are to be performed: *Ralli Bros v Compania Naviera Sota y Aznar*. For example, where payment under an on-demand bond has been prevented by the local courts in which the bank is situated: *AES-3C Maritza East 1 Food v Crédit Agricole Corporate and Investment Bank*.
- **Supervening impossibility.** Impossibility may also engage the doctrine of frustration, particularly where it involves a change to or destruction of the subject matter of the contract, such as the destruction of a building on which work is to be carried out: *Appleby v Myers*. However, not all impossibility engages the doctrine. Impossibility as a result of financial hardship will not. Nor will matters for which a party has agreed to bear the risk of. For example, an EPC Contractor will not be relieved of its obligations if the design of a chemical plant in accordance with the contractual requirements proves to be impossible.
- **Change of circumstances.** This is a more general category which deals with cases where performance is still legal and possible, but circumstances have intervened to radically alter the basis of the contract. One often quoted example is *Krell v Henry* where the English Court of Appeal held that a contract to hire a flat in Pall Mall for the two days of King Edward VII's coronation procession had been frustrated when the coronation was postponed. The Court of Appeal noted that the ability to view the procession was a “state of things assumed by both contracting parties as the foundation of the contract”.

The unifying principle behind these different emanations of the doctrine, as laid down by the English House of Lords in *Davis Contractors Ltd v Fareham Urban District Council*, is that of a “radical change” to the performance called for by the contract such that a party may justifiably say: “it was not this that I promised to do”. As further explained by the Court of Appeal in *The Sea Angel*:

“Among the factors which have to be considered are the terms of the contract itself, its matrix or context, the parties knowledge, expectations, assumptions

and contemplations, in particular as to risk, as at the time of contract, at any rate so far as these can be ascribed mutually and objectively, and then the nature of the supervening event, and the parties’ reasonable and objectively ascertainable calculations as to the possibilities of future performance in the new circumstances. Since the subject matter of the doctrine of frustration is contract, and contracts are about the allocation of risk, and since the allocation and assumption of risk is not simply a matter of express or implied provision but may also depend on less easily defined matters such as ‘the contemplation of the parties’, the application of the doctrine can often be a difficult one. In such circumstances the test of ‘radically different’ is important: it tells us that the doctrine is not to be lightly invoked; that mere incidence of expense or delay or onerousness is not sufficient; and that there has to be as it were a break in identity between the contract as provided for and contemplated and its performance in the new circumstance.”

The doctrine of frustration can be excluded by express contractual provisions which allocate the risks of certain types of events to one of the parties. Or clauses can be drafted in suitably wide terms to eliminate the doctrine of frustration altogether (save in relation to illegality). Conversely, parties may seek to supplement the common law doctrine of frustration by including bespoke “force majeure” clauses. Such clauses are frequently used in English law contracts and are also present in the FIDIC form (now referred to as “Exceptional Events” in the 2nd Editions).

Express force majeure clauses will often define the events or categories of events to which they apply, but may also define a general concept of force majeure (as in FIDIC). Or the term may be left entirely undefined. In the English case of *Lebeaupin v Richard Crispin & Co* the following statement of the meaning of “force majeure” in French law by Goirand was said to be applicable to many English contracts:

“Force majeure. This term is used with reference to all circumstances independent of the will of man, and which it is not in his power to control ... thus, war, inundations and epidemics are cases of force majeure; it has even been decided that a strike of workmen constitutes a case of force majeure.”

Generally, however, the concept of “force majeure” under English law will also import a requirement that the event in question be unforeseeable. In the FIDIC form, this requirement is reflected in the condition that a Force Majeure Event / Exceptional Event be one which could not reasonably have been provided against before entering into the Contract.

As is to be expected the Covid-19 pandemic has seen a number of cases come before the English courts where relief is claimed either under an express force majeure clause or the common law doctrine of frustration. In *Dwyer (UK Franchising) Limited v Fredbar Limited*, a clause in a franchise agreement gave the franchisor the power to designate whether an event which the franchisee claimed to have prevented performance was a force majeure event. Applying established principles of English law, the court found that the franchisor's power to designate was subject to implied obligations to exercise the power honestly, in good faith and genuinely:

"It must not be exercised arbitrarily, capriciously, perversely or irrationally. The [franchisor] in exercising that power must have taken account of the matters which are relevant and ought to be taken into account and not have taken into consideration those matters which are irrelevant. Providing that is done, the decision is one for the [franchisor's] discretion but the court will set it aside if it is one which no reasonable decision-maker could have reached."

The franchisee had complained both about the general impact of the Covid-19 pandemic but also more specifically about the need for a family member to isolate due to medical advice. The franchisor had rejected the existence of a force majeure event in relation to the pandemic generally, but did not specifically address the franchisee's family situation. This was a breach of the implied term.

Of particular note, the court determined that the force majeure clause was a fundamental term of the franchisee agreement and its breach by the franchisor therefore gave rise to a right to terminate the agreement at common law for repudiation:

"In my judgment, looking at the position at the time the Agreement was made, this was a fundamental term. Its application would only arise in exceptional circumstances but that did not mean its exercise was not essential when those circumstances occurred. Plainly it was and a decision by the [franchisor] which ignored an important consideration, in this case the potential effect on [the franchisee's family], would commercially and objectively be considered a breach of an important term which went to the root of the commercial purpose of the Agreement."

A number of cases have concerned the airline industry given the particularly acute effect of the pandemic on travel. In *Salam Air SAOC v Latam Airlines Group SA*, Salam had agreed to lease 3 aircraft from Latam on dry leases (i.e. with Latam merely warranting quiet

possession). Salam was a local cut-price Omani airline and its business was severely affected by local restrictions enacted by the Omani government at the beginning of the Covid-19 pandemic. Initially these prevented any international arrivals, but were subsequently extended to all air travel within Oman except for certain cargo flights.

Salam claimed that the aircraft leases had been frustrated by the change in circumstances relying in particular on the fact that its business plans had been shared by Latam (drawing a comparison with the "frustration of purpose" held in *Krell v Henry*). Latam relied on clause 8.2 of the leases which provided that Salam's obligation to make payment under the leases was "absolute and unconditional irrespective of any contingency whatever" including "any unavailability of the Aircraft for any reason including any lack or invalidity of title or any other defect in the title, airworthiness, merchantability, fitness for any purpose, condition, design or operation of any kind or nature of the aircraft or the ineligibility of the aircraft for any particular use or trade or for registration or documentation under the law of any relevant jurisdiction, or the Total Loss of, or any damage to, the Aircraft."

This clause was sufficient to debar any claim for frustration in relation to the pandemic. The risk that Salam would be unable to undertake passenger flights within Oman or that there would be a long lasting fall in demand for such flights was a risk that Salam had expressly accepted. The breadth of the clause was highlighted by the fact that total destruction of the aircraft or dispossession through a requisition of title was not to affect payments under the lease.

A similar result was achieved in *Wilmington Trust SP Services (Dublin) Limited v Spicejet Limited* where three aircraft had also been leased under dry leases for 10 years each. The use of one aircraft was heavily curtailed due to restrictions imposed by the Indian government as a result of the pandemic. The other two had been grounded due to fatal crashes of similar aircraft due to design defects. The leases had very similar clauses to that considered in *Salam Air* making payment under the leases unconditional on any inability to use the aircraft.

Spicejet, the leasee, claimed that an implied right to suspend the payment of rent existed in relation to the aircraft whose use had been curtailed by law. However, such a right was found to be clearly inconsistent with the payment clause. The leases in relation to the two grounded aircraft were said to have been frustrated, but again this argument ran into the very broad wording of the payment clauses. However, without deciding the matter, the court indicated that the fact that the



grounding related to inherent defects in the aircraft themselves may take the case outside the payment clause, but in that case the period of grounding would be important. At the time of judgment, the aircraft had been grounded for only one year of the 10 year period. In the court's view:

"It may be (I express no view one way or the other) that if there is still no sign of the ban being lifted in say, three years' time, that might amount to frustration. But in the context of a ten-year lease, I find it very difficult to say that a suspension of use for roughly 10% of the term of the lease amounts to a change in circumstances which renders performance of the lease 'radically different' rather than simply more onerous."

Another recent case of note is *MUR Shipping BV v RTI Ltd*. This case concerned a contract of affreightment which required the charterer to pay the owner freight in US dollars. Part way through the contract, the United States Government applied sanctions to the charterer's parent company meaning that payment under the contract in US dollars was no longer possible (as such payments would need to be cleared through a US bank). The charterer offered to make payment in Euros instead and to make good any exchange losses suffered by the owners in converting payment into US dollars. The owner's rejected this proposal and invoked the

provisions of a force majeure clause under the contract. The charterers were required to make alternative arrangements and sued the owner for increased costs incurred as a result.

The dispute was referred to arbitration and the arbitrators upheld the owner's reliance on the force majeure clause save in one respect. The clause required that any force majeure event should not be capable of being "overcome by reasonable endeavours from the Party affected". The arbitrators accepted the charters argument that the owners ought to have accepted their proposal to pay in Euros, particularly as it would have caused no detriment to the owners.

This aspect of the arbitration award was overturned on appeal to the English Commercial Court. Clarifying previous decisions on this point, the court confirmed that: "*a party is not required, by the exercise of reasonable endeavours, to accept non-contractual performance in order to circumvent the effect of a force majeure or similar clause. ... a relevant contractual obligation is not simply a factor to be weighed in the balance when coming to an overall assessment of reasonableness.*" Accordingly, the owners were entitled to insist on payment in US dollars as a matter of right and to claim relief under the force majeure clause as a consequence.

Singapore

Although not related to the Covid-19 pandemic a decision of the High Court of Singapore last year provides an interesting contrast in approach to the interpretation of a force majeure clause using the term “force majeure” without further elaboration (as is done in the commonly used UK standard form, the JCT).

GTMS Construction Pte Ltd v Ser Kim Koi concerned a final account dispute in relation to a residential development in Singapore. The force majeure issue arose in the context of an extension of time claimed for by GTMS in respect of electrical connection works carried out by the electrical utility. The utility had identified the need for an overground connection box (an “OG Box”) at late notice and time was needed to agree a location for this. The utility’s work was also delayed more generally for a range of reasons including adverse weather and issues with its own subcontractors.

GTMS relied on an extension of time clause in the building contract which allowed time for delays to completion caused by “force majeure”. The contract did not provide any definition of “force majeure” and the court therefore set out the approach under Singaporean law to the meaning of that term. Drawing from previous authorities, the court concluded that the term referred to “an event that impedes or obstructs the performance of the contract, which was out of the parties’ control and occurred without the fault of either party.” In contrast with English law, however, the court rejected the employer’s argument that unforeseeability was a requirement. Previous cases had:

“distinguished the concept of force majeure from the related doctrine of frustration, in which the element of unforeseeability is critical. However, a force majeure event is typically ‘radical’ ... Borrowing from the doctrine of frustration, this refers to where ‘the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract’ (see Davis Contractors Ltd v Fareham Urban District Council)”

This distinction was crucial to the court’s decision in relation to the delays brought about by the OG Box and the electrical utility. The court found that these delays had occurred without the fault of either party and were outside their control. However, the employer claimed that the delays were foreseeable, noting that a large allowance for the utility’s works had been included in the master programme which had specifically intended to cater for delays in the power connection works.

In the court’s judgment, this did not prevent the delays from being “radical” and thereby qualifying as a force majeure event:

“... as I have observed above, the element of foreseeability is not critical to the concept of force majeure. Instead, the true question is whether the event was such that it rendered performance of the contract ‘radically different’ from what was originally undertaken. In my view, it was. [The utility] had initially estimated that it would take about four to six weeks to complete its power connection works [when it] would typically take a much shorter time of about two weeks. However, the actual time between when [it] was first notified ... and when power connection works were eventually completed ... was around 19 to 21 weeks. While parties did anticipate some delay to be possible, this was significantly longer than what all parties had expected. ... Therefore, although some delays were expected from SPPG, the extent of the delay in this case was so protracted that it rendered the performance of the Contract radically different from what had initially been undertaken. The same can be said for the last-minute introduction of the OG Box requirement.”

On the face of it, this decision appears to give a rather generous meaning to the test of “radical difference”. As the court notes, this test has been borrowed from the doctrine of frustration under English law, which sets a very high bar. The *Davis Contractors* case cited by the court is the leading English case on frustration and itself concerned delays under a construction contract. Work in that case which had intended to complete within 8 months eventually took 22 months due partly to bad weather, but also to an unforeseen shortage of labour due to an unexpected lag in the demobilisation of troops after the Second World War. Such delays were, however, still not sufficient to make the contract radically different from what was intended. As Lord Reid noted, “the delay was greater in degree than was to be expected. ... the job proved to be more onerous but it never became a job of a different kind from that contemplated in the contract”. Similar comments could, perhaps with even greater force, be made of the situation in *GTMS Construction*.

Overall, therefore, Singapore appears to have taken a comparatively liberal approach to the meaning of the phrase “force majeure”. One which does not require unforeseeability, but which emphasises a concept of “radical difference” considerably more lenient than that found in the English cases.



United States of America

The general law rules for frustration in the USA bear some similarity to English law, but owe their origin more to the concept of force majeure under the French Civil Code. Originally, they emphasised relief from events which rendered performance "impossible", but have since broadened to include the concept of "practical impossibility". A classic statement of the law comes from *Transatlantic Financing Corp v US*:

"The doctrine of [practical impossibility] ultimately represents the ever-shifting line, drawn by courts hopefully responsive to commercial practices and mores, in which the community's interest in having contracts enforced according to their terms is outweighed by the commercial senselessness of requiring performance ... When the issue is raised, the court is asked to construct the condition of performance based on the changed circumstances, a process which involves at least three reasonably definable steps. First a contingency – something unexpected – must have occurred. Second, the risk of the unexpected occurrence must not have been allocated either by agreement or by custom. Finally, the occurrence of the contingency must have rendered performance commercially impracticable. Unless the court finds these three requirements satisfied, the plea of impossibility must fail."

Mere financial difficulty is insufficient to engage the rule: *"Economic hardship, even to the extent of bankruptcy or insolvency, does not excuse performance."* (*Ebert v Holiday Inn*).

In determining how impractical performance must be before it is deemed to be "practically impossible", some similarities with the English law concept of "radical difference" can be observed. In *Northern Corp v Chugach Electric Association*, a contract for the repair of a dam was let on the assumption that an access route would be available across a frozen reservoir in Winter rather than cut through the mountainous terrain which surrounded the reservoir. The actual Winter conditions following the contract were unexpected and did not permit access across the reservoir. The Supreme Court of Alaska found the contract to be frustrated, despite the theoretical possibility of cutting a route through the mountains. In the Court's view, quoting Professor Williston: *"the important question is whether an unanticipated circumstance, the risk of which should not fairly be thrown upon the promisor, has made performance of the promise vitally different from what was reasonably to be expected"*.

A recent application of these principles arising from the Covid-19 pandemic is *Latino v Clay LCC*. In that case a gym business suffered from a lack of custom during the

pandemic with a consequent loss in cashflow and meaning that certain payments were unable to be met. The gym's defence of frustration was rejected on the basis that the doctrine did not apply to economic hardship.

More controversial is whether a doctrine of "frustration of purpose" exists beyond questions of impossibility or impracticability – in a similar way to the English decision of *Krell v Henry*. Such a doctrine is found in the Restatement Second, Contracts § 265 which reads as follows:

"Where, after a contract is made, a party's principal purpose is substantially frustrated without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his remaining duties to render performance are discharged, unless the language or the circumstances indicate the contrary."

Despite its presence in the Restatement, this broader doctrine has not commanded general acceptance before the US courts. However, one recent example of its application arising from the pandemic is *Banco Santander (Brasil) SA v American Airlines Inc*. The case concerned an agreement between Santander and American Airlines to jointly market a credit card with a frequent flyer rewards programme. Santander was required to pay American Airlines for rewards points earned by its customers and committed to pay a minimum amount regardless of the number of points earned. The pandemic resulted in American Airlines cancelling all flights to Brazil and Santander claimed that this had rendered the contract valueless to it, given that rewards points would now be of no value to its customers. It therefore claimed to be released from its obligations under the contract as a result of the doctrine of frustration of purpose. The court refused to strike out this defence as a matter of law, finding that it could in principle succeed subject to questions of foreseeability and whether the contract had in fact become valueless to Santander.

Express force majeure clauses are very common in US law contracts and allow greater specificity to be applied to the doctrines discussed above. However, boilerplate clauses which refer merely to "force majeure" are likely to be interpreted purely as confirming the general law: *"merely reciting 'force majeure' in a contract ... invokes a body of common law doctrine interpreting the term that is largely indistinguishable from the doctrine of impossibility (or impracticability)" (Commonwealth Edison Co v Allied-General Nuclear Services).*

Australia

The English *Davis Contractors* decision has been adopted by the High Court of Australia and the "radical change" test therefore applies to arguments of frustration in Australia. A recent application of these principles in the circumstances of the Covid-19 pandemic arose in *Dyco Hotels Pty Ltd v Laundry Hotels (Quarry) Pty Ltd*. The case concerned the sale of a hotel, which included a restaurant and other facilities. The purchase price was USD 11.25m, of which USD 750,000 was allocated to goodwill of the hotel business. The sale contract contained an obligation on the owner to continue trading in the usual and ordinary course up until completion of the sale (roughly two months after the date of the contract), but the owner gave no warranty as to the level of income which could be expected from the hotel business.

Approximately a week before completion was due to take place, public health restrictions were imposed by the New South Wales government as a result of the pandemic. These prevented the ordinary continuation of the hotel business, save for takeaway food orders. The purchaser claimed that the introduction of the restrictions had frustrated the sale contract.

The court found that the restrictions had not prevented the performance of the sale contract. The obligation to continue trading was subject to an implied qualification that trade be carried out in a lawful manner. The question was therefore whether the restrictions amounted to such a radical change that the contract was frustrated despite there being no legal or practical impediment to it being carried out. As the court noted:

"It is necessary to consider whether these unexpected events gave rise to a fundamental commercial difference between the actual and contemplated performance of the contract, or a fundamentally different situation for which the parties made no provision, such that it would not be just to hold the parties bound to the terms of the contract. Or, as Lord Reid put it [in Davis Contractors], the question can be posed as [to] whether the contract is on its true construction wide enough to apply to the new situation."

A key consideration in the court's judgement was the disclaimer of any warranty by the owner as to the levels of income which could be expected from the business. That indicated *"that insofar as the public health orders may have had an adverse effect upon the financial performance of the Business after settlement, that is a risk of a type the plaintiffs were apparently prepared to take, even if the actual circumstances that unfolded were not foreseen by them at the time of contract."*

The purchaser might presumably have responded that it had only accepted the risk of income fluctuations in the normal course of things and not from any eventuality whatsoever, no matter how unexpected or unusual. Nevertheless, the conclusion shows the importance that agreed contractual terms and risk allocations can have on frustration arguments.

The court distinguished the case from a previous decision where the sale of a dairy farm had become frustrated by supervening legislation which abolished an existing milk quota scheme. The quota allocated to the dairy farm had been part of the assets to be sold under the agreement and the legislation therefore affected the assets themselves. By contrast, the hotel and its business remained unchanged, but was merely less valuable in light of the public health restrictions which had been imposed. This was a risk that the purchaser was prepared to take. At all events, the situation was not so radical or fundamentally different *“that it would not be just to hold the parties bound to the terms of the contract”*.

Conclusions and implications

A number of observations can be drawn from the above survey. Perhaps the clearest of all is the lack of success with which parties have argued for the application of general doctrines of frustration. In no case were such arguments successfully deployed and whilst Santander survived a strike out motion on such an argument, it remains to be seen whether it will be able to establish its position at trial. Frustration defences remain a “last resort” and their difficulty should not be underestimated.

It may also be observed that the types of frustration arguments raised were “change of circumstance” or “frustration of purpose” arguments rather than illegality or impossibility type arguments. Such frustration arguments are the more difficult to establish, assuming they are available at all in the jurisdiction concerned. Such arguments are also much more sensitive to the terms and conditions of the existing contract, with the court keen to identify any indication of contractual intent which might be said to have a bearing on the type of event which has occurred. *Dyco Hotels* provides a good illustration of how far agreed allocations of risk can be said to extend in this regard.

As one might expect, greater success has been had with arguments under express “force majeure” clauses but a large variation in approach exists to the interpretation of such clauses, particularly where the term “force majeure” is used without elaboration. In England, the term is given a broad interpretation; essentially any unforeseeable event outside the control of the parties. The approach in Singapore, emphasising radical change

over unforeseeability, appears to align itself more closely with frustration, albeit with a very generous application of what amounts to “radical” in the case considered above. The Singaporean approach to the term “force majeure” receives support from the US cases where the term is equated with general law notions of “practical impossibility” and a “vital difference” in circumstances.

The finding in *Dwyer* that a force majeure clause was a fundamental term is also of note, as this gives the innocent party an immediate right to terminate for breach under English common law. This should be borne in mind where, as in *Dwyer*, a clause envisages some positive role for the employer in verifying or certifying that a force majeure event has occurred.



References:

Krell v Henry [1903] 2 KB 740; *Lebeaupin v Richard Crispin & Co* [1920] 2 KB 714; *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696; *Transatlantic Financing Corp v US* 363 F.2d 312, 3 UCC Rep Serv 401 (DC Cir 1966); *Northern Corp v Chugach Electric Association* 518 P.2d 76, modified on rehearing, 523 P.2d 1243 (Alaska 1974); *Commonwealth Edison Co v Allied-General Nuclear Services* 731 F.Supp 850 (ND Ill 1990); *Ebert v Holiday Inn* 628 F App'x 21 (2d Cir 2015); *AES-3C Maritza East 1 Eood v Crédit Agricole Corporate and Investment Bank* [2011] EWHC 123; *Salam Air SAOC v Latam Airlines Group SA* [2020] EWHC 2414 (Comm); *Lantino v Clay LLC* (2020) 1:18-cv-12247; *Dwyer (UK Franchising) Limited v Fredbar Limited* [2021] EWHC 1218 (Ch); *Wilmington Trust SP Services (Dublin) Limited v Spicejet Limited* [2021] EWHC 1117 (Comm); *Dyco Hotels Pty Ltd v Laundry Hotels (Quarry) Pty Ltd* [2021] NSWSC 504; *GTMS Construction Pte Ltd v Ser Kim Koi* [2021] SGHC 9; *GTMS Construction Pte Ltd v Ser Kim Koi* [2021] SGHC 9; *Banco Santander (Brasil) SA v American Airlines Inc* (2021) 1:20-cv-03098; *MUR Shipping BV v RTI Ltd* [2022] EWHC 467 (Comm).

Limitation of liability in construction contracts: the relevance of intentional or repudiatory breaches

A recent decision of the English Technology and Construction Court (the TCC) has considered the interpretation of a limitation of liability clause in the context of an international construction project in the Falkland Islands. The decision seeks to resolve conflicting case law as to whether any interpretative presumption exists against the exclusion or limitation of liability for deliberate breaches of contract. The case also highlights the benefits of using a cap on liability rather than a total exclusion where very broad clauses are concerned.



An interpretive presumption against intentional and deliberate breaches?

The leading authorities on exclusion and limitation clauses under English law are the *Suisse Atlantique* and *Photo Production* cases, in which the English House of Lords rejected the so-called doctrine of fundamental breach which disabled a party from relying on an exclusion clause where a contract had been brought to an end as a result of a fundamental breach of contract, such as by repudiation. Instead, it was held that whether an exclusion clause was to be applied to any given breach of contract was a matter purely of contractual interpretation.

In a well-known passage from *Suisse Atlantique*, Lord Wilberforce noted that the usual rules of contractual interpretation meant “*the more radical the breach the clearer must the language be if it is to be covered*”. Lord Wilberforce also noted that very broad clauses would be given a narrow interpretation if they would otherwise deprive one party’s obligations of all contractual force, as “*to do so would be to reduce the contract to a mere declaration of intent*”.

Whether the requirement for clear language in relation to radical breaches gives rise to an interpretative presumption has been considered in subsequent cases including in relation to deliberate and intentional breaches. In *Internet Broadcasting Corporation Ltd & others v MAR LLC (Marhedge)*, a Deputy Judge held that there was a strong presumption that an exclusion clause would not be found to cover a deliberate repudiatory breach of contract and that the presumption could only be rebutted by strong and explicit language. This differs from the decision in *AstraZeneca UK Ltd v Albemarle International Corp* where the English High Court held that the correct approach was “*simply one of construing the clause, albeit strictly, but without any presumption*.” The judge in that case, Mr Justice Flaux, went on to state that he considered the decision in *Marhedge* to be wrong on the basis it sought to revive the doctrine of fundamental breach which the House of Lords had concluded was no longer good law in *Photo Production*.

Similar issues were considered by the Court of Appeal in *Kudos Catering (UK) v Manchester Central Convention Complex*. A five-year exclusive supply agreement for catering services at two large convention centres contained a broad exclusion of any liability for loss of business, revenue or profits in favour of the operator of the centres. The operator was alleged to have repudiated the agreement and at first instance the exclusion clause was held to defeat a claim for loss of profits for the remaining period of the agreement. The Court of Appeal overturned this finding, deciding the

clause should be read as applying only to claims arising in the performance of the agreement, not its repudiation. If an exclusion of all liability for financial loss in the event of a repudiation by the owner had been intended, the Court “*would have expected them to spell that out clearly, probably in a free-standing clause*”. The Court rejected the suggestion that its approach was a resort to the doctrine of fundamental breach overruled in *Photo Production*. Rather, it was: “*a legitimate exercise in construing a contract consistently with business common sense and not in a manner which defeats its commercial object. It is an attempt to give effect to the presumption that parties do not lightly abandon a remedy for breach of contract afforded them by the general law.*” A similar conclusion was reached by the Court of Appeal in *Transocean Drilling v Providence Resources* where a broad exclusion clause covering loss of revenue and loss of profit was said not to contemplate a deliberate repudiation of the contract.

Mott MacDonald Ltd v Trant Engineering Ltd

In this most recent case, Trant, an engineering contractor, engaged Mott MacDonald (MM) for design consultancy services in connection with the construction of a new power station at a military base in the Falkland Islands. Following an initial dispute, the parties entered a Settlement and Services Agreement (SSA) to resolve the existing dispute and govern the parties’ obligations on the project going forward. The SSA contained a total cap on liability of GBP 500,000, exclusions on liability and a net contribution clause.

Following Trant’s failure to make certain payments, MM commenced proceedings. Trant counterclaimed for GBP 5m alleging that MM had “*fundamentally, deliberately and wilfully*” breached the SSA by a refusal to perform. MM denied the breach, but contended that even if Trant could prove breach, and those breaches were deliberate and fundamental, the exclusion and limitation clauses in the SSA would still apply.

No presumption

The TCC granted summary judgment for MM on this issue. Judge Eyre QC recognised the stark contrast between the approaches in *Marhedge* and *AstraZeneca* and concluded that the Deputy Judge in *Marhedge* had erred in his analysis of the true effect of the House of Lords authorities. The judge endorsed the position set out in *Photo Production* and as summarised in the *AstraZeneca* case, notably that exclusion clauses including those purporting to exclude or limit liability

for deliberate and repudiatory breaches are to be construed by reference to normal principles of contractual construction without the imposition of a presumption and without requiring any particular wording to achieve the effect of excluding liability. This finding was subject to the proviso that an exclusion or limitation of liability will not be read as operating to reduce a party's obligations to the level of a mere declaration of intent.

Following this approach, the judge found that the clauses in the SSA were in clear terms and capable of applying to the alleged breaches, noting that the SSA was a bespoke agreement intended to be a comprehensive regulation of the parties' future dealings.

The judge considered whether a deliberate breach would leave the exclusion and limitation clauses commercially nonsensical or such as to reduce MM's obligations to a mere declaration of intent. On the facts the judge was satisfied that the presence of the GBP 500,000 liability cap made the latter impossible on the basis that, in the event of a repudiatory breach accepted by Trant as terminating the SSA, MM would remain liable up to the level of the cap.

Conclusions and implications

This decision is significant for its analysis of conflicting previous decisions as to the interpretation of exclusion and limitation clauses in relation to deliberate and intentional breaches of contract. The court's refusal to apply a presumption against the application of these clauses to such breaches appears to accord with a more general trend in recent times towards allowing such clauses to speak for themselves without presumptive fetters.

The court's judgment does not refer to either of the Court of Appeal's decisions in *Kudos* or *Transocean*. It remains to be seen, therefore, how the court's decision is to be reconciled with the conclusion in those cases, expressed in presumptive language, that repudiatory breaches would fall outside an otherwise generally worded exclusion clause.

Parties should also be aware that courts will generally construe exclusions more strictly than limitations and care should be taken where agreeing exclusion clauses that deprive one party's obligations of all contractual force. One key reason for the court upholding the limitation clause in the present case was that MM retained liability to a certain extent up to the GBP 500,000 cap, making arguments as to commercial absurdity and "mere declarations of intent" much more difficult.

References:

Suisse Atlantique Societe d'Armement Maritime SA v N V Rotterdamsche Kolen Centrale [1967] 1 AC 63; *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827; *Internet Broadcasting Corporation Ltd v MAR LLC* [2009] EWHC 844 (Ch); *AstraZeneca UK Ltd v Albemarle International Corporation* [2011] EWHC 1574 (Comm); *Kudos Catering (UK) Ltd v Manchester Central Convention Complex Ltd* [2013] EWCA Civ 38; *Transocean Drilling UK Ltd v Providence Resources Plc* [2016] EWCA Civ 372; *Mott MacDonald Ltd v Trant Engineering Ltd* [2021] EWHC 754 (TCC).





Parent company guarantees as on-demand bonds: a softening of the English law approach

An English Court of Appeal decision last year marks a significant shift in the English law approach to the interpretation of guarantees. The decision has distanced the English law approach from a presumption against an on-demand interpretation where the surety is not a financial institution such as a bank or insurance company. Instead, the focus is to be on the words used regardless of the identity of the surety. The decision makes it more likely that parent company guarantees will be found to be truly on-demand and should be borne in mind by those involved in negotiating such instruments.



On-demand vs “see to it” guarantees

The difference between guarantees and on-demand bonds can be difficult to determine. Both are used to guard against the possibility of non-performance of a contractual obligation. However, the protection afforded by each is different.

A guarantee usually creates a secondary obligation, under which the guarantor guarantees the performance of a primary obligation under the underlying contract (this is sometimes referred to as a “see to it” guarantee). The liability of the guarantor is therefore dependent on the performance of the primary obligation. Whilst “primary obligor” wording in such guarantees can result in the guarantor undertaking primary obligations, the guarantor’s liability will remain dependent on whether or not there has been a breach of the underlying contract.

By contrast, a truly “on-demand” bond imposes a primary obligation on the guarantor to pay the beneficiary of the bond immediately upon receipt of a demand for payment. Payment by the guarantor is not contingent on performance of the underlying contract or proof of loss. Typically, a simple statement detailing that an obligation in the underlying contract has been breached and that loss has been suffered by the beneficiary is sufficient to trigger payment. There is no need to prove either breach or loss.

Paget’s formula

Historically, English law has used a set of rules drawn from banking law to decide whether or not a bond is on-demand (with terms such as ‘guarantee’ not being determinative). Many of these rules are aimed at determining whether the bond provider’s liability is intended to be secondary in relation to the underlying contract (and thereby conditional) or primary. In relation to international transactions, *Paget’s Law of Banking*, 15th edition, states:

“Where an instrument: (i) relates to an underlying transaction between parties in different jurisdictions; (ii) is issued by a bank or other financial institution; (iii) contains an undertaking to pay ‘on demand’ (with or without the words ‘first’ and/or ‘written’); and (iv) does not contain clauses excluding or limiting the defences available to a surety, it will almost always be construed as a demand guarantee. By contrast, where an instrument is not given by a bank or other financial institution it has been held that there is a strong presumption against it being construed as a demand bond.”

To this list one might add where payment is to be made based upon a certificate or other documents rather than facts (*IE Contractors v Lloyds Bank*).

The formulation from Paget’s has received judicial approval on a number of occasions, although it was accepted early on that item (iv) was not conclusive. As noted by the Court of Appeal in *Gold Coast Ltd v Caja De Ahorros*, there are:

“reasons for including [clauses excluding or limiting the defences available to a guarantor] in an instrument which is intended to be autonomous. It might, for example, have been included to avoid any argument that variation of the [underlying] contract ... would imperil recovery under the ... guarantees. It could have been inserted simply to ensure that the rule applicable to true guarantees did not apply to this instrument.”

This also accords with our experience of truly on-demand bonds being drafted with very detailed clauses excluding or limiting the defences available to the issuing bank. Nonetheless, such clauses will weigh against the finding of a truly “on demand” obligation where the operative parts of the bond are not drafted with clarity (see for example *Trafalgar House Construction v General Surety and Guarantee*).

The status of the issuer

Item (ii) from Paget’s formulation has been subject to debate for some time. By way of background, the relatively early decision in *Esal Commodities v Oriental Credit CA* provides an example of the issuer’s status as a bank being used for the purpose of interpretation. The document in that case was described as a “performance bond” for 10% of the contract price and was held to be payable on-demand despite express words which suggested conditionality. The bond was payable “on your written demand in the event that the supplier fails to execute the contract in perfect performance...” The surrounding circumstances, including the fact that the document was issued by a bank, made it sufficiently clear that the instrument was intended to provide prompt and certain payment in the manner of an on-demand bond.

The reason why such a generous interpretative approach is taken to bonds issued by banks as opposed to other entities was explained by Hirst J in *Siporex Trade SA v Banque Indosuez*:

"There is in my judgment no real hardship on the bank in imposing this strict liability to pay. A performance bond is a commercial instrument. No bank is obliged to enter into it unless they wish to and no doubt when they do so, they properly exact commercial terms and protect themselves by suitable cross-indemnities ..."

Very different considerations apply to the interpretation of bonds issued between parties or their related entities. In *Marubeni Hong Kong v Government of Mongolia* the Court of Appeal noted that the cases involving banks, *"provide no useful analogy for interpreting a document which was not issued by a bank and which contains no overt indication of an intention to create a performance bond or anything analogous to it."* In that case, the Mongolian Ministry of Finance (for commercial trading reasons it would appear) had *"unconditionally pledge[d] to pay to you upon your simple demand all amounts payable under the Agreement if not paid when the same becomes due..."* Despite the similarity of this wording to the performance bond in *Esal*, the Court of Appeal declined to find an on-demand obligation, finding instead that the promise was in the nature of a guarantee and conditional upon proof of default. The court held that for bonds issued outside of a banking context, there was a strong presumption against their being on-demand as opposed to conditional.

"Turning to the [guarantee], the starting-point in my view is that it is not a banking instrument, and it is not described ... in terms appropriate to a demand bond or something having similar legal effect. ... The terminology is not of course conclusive. However, I agree ... that, if MHK had wanted the additional security of a demand bond, one would have expected them to have insisted on appropriate language to describe it, in ... the instrument itself ... The absence of such language, in a transaction outside the banking context, creates in my view a strong presumption against MHK's interpretation [i.e. that the guarantee was truly on-demand]."

A similar result was achieved in *Vossloh AG v Alpha Trains (UK) Ltd*. The claimant provided a parent company guarantee in favour of the defendant, which guaranteed the performance of the contracted works. The defendant subsequently alleged defective work and made a call on the guarantee. Despite the fact that amounts were said to be payable 'on demand', the court applied the presumption from *Marubeni* to interpret the instrument as a conditional bond requiring proof of default.

Wuhan Guoyo Logistics Group v Emporiki Bank of Greece

The strength of the presumption in the opposite direction for guarantees issued by banks was squarely tested in *Wuhan Guoyo Logistics Group Co Ltd v Emporiki Bank of Greece SA* decided in 2012. Although expressed to be "on demand" the wording of the guarantee in that case gave a number of indications which supported a conditional interpretation requiring proof of default. Key parts of the wording were as follows:

"DETAILS OF GUARANTEE

Dear Sirs,

1) ... we ... **IRREVOCABLY, ABSOLUTELY and UNCONDITIONALLY** guarantee, as the primary obligor and not merely as the surety, the due and punctual payment by the BUYER of the 2nd instalment of the Contract Price ...

...

(3) We also **IRREVOCABLY, ABSOLUTELY and UNCONDITIONALLY** guarantee, as primary obligor and not merely as surety, the due and punctual payment by the BUYER of interest on the second Instalment guaranteed hereunder ...

(4) In the event that the BUYER fails to punctually pay the second Instalment guaranteed hereunder or the BUYER fails to pay any interest thereon, and any such default continues for a period of twenty (20) days, then, upon receipt by us of your first written demand stating that the Buyer has been in default of the payment obligation for twenty (20) days, we shall immediately pay to you or your assignee the unpaid 2nd Instalment, together with the Interest as specified in paragraph (3) hereof, without requesting you to take any or further action, procedure or step against the BUYER or with respect to any other security which you may hold.

....

(7) Our obligations under this Guarantee shall not be affected or prejudiced by any disputes between you as the SELLER and the BUYER under the Shipbuilding Contract or by the SELLER's delay in the construction and/or delivery of the VESSEL due to whatever causes or by any variation or extension of their terms thereof or by any security or other indemnity now or hereafter held by you in respect thereof, or by any time or indulgence granted by you or any other person in connection therewith, or by any invalidity or unenforceability of the terms thereof, or by any act, omission, fact or circumstances whatsoever, which could or might, but for the foregoing, diminish in any way our obligations under this Guarantee."

The judge at first instance, Christopher Clarke J, identified a number factors in favour of a conditional interpretation including:

- The instrument was referred to as a “guarantee” not an “on-demand” instrument.
- Clauses 1 and 3 expressly guaranteed the “due and punctual payment” of the 2nd installment and interest respectively.
- The payment obligation in clause 4 was said to apply “in the event that the Buyer fails punctually to pay the second instalment”.
- Clause 7 sought to exclude the defences available to the guarantor within the meaning of paragraph (iv) of *Paget’s* formula.

By contrast, the factors in favour of an on-demand interpretation were as follows:

- Clause 4 requires payment to be made “on first written demand” and specifies that the demand must state that the Buyer has been in default for 20 days.
- Payment is to be made “immediately” without any request being made to the Seller to take any action against the Buyer.
- Clause 7 provides that the guarantor’s obligations are not to be affected or prejudiced by any dispute between the Seller and the Buyer in relation to the underlying transaction.
- Clause 10 (not quoted above) imposed a monetary limit on the bond equivalent to the second instalment plus interest for 60 days, indicating there was not intended to be any great delay in payment after default.

The guarantor was a financial institution, the Bank of China, but was not charging a fee for the guarantee as it had a direct connection with the underlying transaction, being the lender to the buyer. The judge did not therefore consider paragraph (ii) of *Paget’s* formula to be engaged. Overall, the judge found the above wording insufficiently clear to give rise to an on-demand obligation.

The judge’s findings were overturned on appeal, principally because he had failed to have sufficient regard for *Paget’s* formulation. Commenting on the factors for and against a conditional interpretation the Court of Appeal considered that:

*“In deciding whether the document is a traditional ‘see to it’ guarantee or an ‘on demand’ guarantee, it would be obviously absurd to say that there are 6 pointers in favour of the former and only 4 pointers in favour of the latter and it must therefore be the former. But if the law does not permit boxes to be ticked in this way, commercial men will need some assistance from the courts in determining their obligations. The only assistance which the courts can give in practice is to say that, while everything must in the end depend on the words actually used by the parties, there is nevertheless a presumption that, if certain elements are present in the document, the document will be construed in one way or the other. It is exactly this kind of assistance that the editors of *Paget’s Law of Banking* have endeavoured to provide.”*

The Court referred to its previous endorsement of *Paget’s* formulation in the cases referred to earlier and found that the judge had given insufficient weight to these authorities. In the Court’s judgment:

*“There were also the positive factors in favour of the document being an on demand guarantee and, granted these positive factors, and the presumption enunciated by *Paget* ... and supported by previous authority, the judge ought in my respectful view to have had much more regard to the presumption than he did. As *Hirst J* said: ‘it is extremely important that ... there should be a consistency of approach by the Courts, so that all parties know clearly where they stand.’”*

Shanghai Shipyard Co v Reignwood International Investment

The Court of Appeal has now revisited the role of *Paget’s* formulation in a decision last year and has interpreted a guarantee given by a parent company as an on-demand instrument. In the process the Court has sought to distance itself from the use of presumptions at all, noting that:

“there ought to be no room for a priori preconceptions or assumptions about the nature of the instrument to be derived from the identity of the guarantor. What matters is the wording in which the parties have chosen to express their bargain, interpreted in accordance with the well-established rules of construction.”

The case concerned a shipbuilding contract in respect of which a guarantee was given in terms largely indistinguishable from those in *Wuhan* quoted above, save that clause 4 contained a proviso in the following terms:



"In the event that there exists a dispute between the Owner and the Builder as to whether [the relevant payment is due] and such dispute is submitted either by the Owner or by you for arbitration in accordance with Clause 17 of the Contract, we shall be entitled to withhold and defer payment until the arbitration award is published. ..."

The guarantee was given by a parent company of the buyer, but the guarantor had only become a parent as a result of a financing arrangement between itself and the buyer. Accordingly, *"it clearly exercised a financing function beyond that which might arise between parent and subsidiary to an established group of companies in relation to the group's business."*

In these circumstances, the judge at first instance reached a similar conclusion to Clarke J in Wuhan but was fortified by the fact that the guarantor was not a financial institution and did not therefore fall within Paget's formulation.

"It is nonetheless important to approach the language of the Guarantee in line with the guidance given by the Court of Appeal in Wuhan. ... in contrast to the facts of Wuhan, the fact that the Guarantee was not issued by a bank takes the present case out of the "presumption" derived from the distinguished banking textbook. ... the current edition of Paget suggests (at footnote 3 to section 35.8) that where an instrument is not given by a bank or other financial institution "[c]ogent indications that the instrument was intended to operate as a demand guarantee will be required ..."

Treating this as part of the assistance offered by the textbook to commercial parties, and having regard to the Court of Appeal's guidance on the importance of consistency, the absence of indications of that strength or quality is material, and adverse to the Builder's contention. ... in my judgment, the language of the Guarantee does not make the grade of a demand guarantee without the help of a presumption ..."

As noted above, the Court of Appeal disagreed with this approach and distanced itself from the use of any presumption. The court noted that, as a matter of counterparty risk, there was no clear line to be drawn between banks and trading companies in terms of financial strength and probity: *"A well-resourced and reputable trading company in an accessible jurisdiction may provide better protection for a beneficiary against counterparty risk than a bank with political affiliations operating in an underdeveloped jurisdiction giving rise to uncertainties of enforcement."*

The court also noted that whether or not a company falls within the category of a financial institution is often not a binary question. Trading companies may, as in this case, have a significant financing role, and banks, as in Wuhan, may be connected with the underlying transaction.

Accordingly, in the Court's view:

"If a non-bank gives a guarantee adopting a form of wording which, if given by a bank, would be a demand guarantee. I do not see how it can mean

something different from an identical instrument if issued by a bank. Such a conclusion would be a receipt for commercial uncertainty and would, in my view, subvert the reasonable expectations of the parties as objectively expressed in the words of their agreement.”

Shorn of any presumption, the Court considered the language of the guarantee to point in favour of an on-demand instrument. The Court noted those factors in support of an on-demand obligation referred to in *Wuhan* but also relied on two further factors:

- The use of the capitalised words “ABSOLUTELY” and “UNCONDITIONALLY” in clauses 1 and 3 were in the Court’s view indicative of on-demand obligations. Although such obligations are strictly speaking not unconditional or absolute (for example, there must be a valid demand and an absence of fraud), such words were likely to convey to an ordinary businessman that the guarantee was not conditional on proof of liability.
- The reference to the guarantee being liable as primary obligor “and not merely as the surety” were said to be a “clear indication” against a conditional guarantee. A conditional guarantee would mean the guarantor was merely a surety.

Conclusion

The Court of Appeal’s decision in *Shanghai Shipyard* marks a fundamental shift in the English law approach to the interpretation of guarantees on international projects. A number of points may be made about the nature of this change:

- The Court’s decision stands in significant conflict with previous Court of Appeal decisions which have supported the use of a presumption by reference to the status of the guarantor. These other cases include *Gold Coast*, *Marubeni* and *Wuhan*. These conflicts are to some extent acknowledged in the Court’s judgment but no real attempt is made to reconcile or distinguish these decisions. This in turn may prove problematic in future cases with each party relying on different Court of Appeal authorities in support of its position. Clarification may be needed from the Supreme Court if the issue is to be satisfactorily resolved.
- The Court’s comment that an identical instrument issued by a non-bank and a bank should have the same meaning is difficult to reconcile with the established approach to the interpretation of contracts under English law. It is uncontroversial that interpretation may be affected by background facts

known to both parties at the time the contract was entered into. There is no reason why these facts should not include the identity of the parties and their business. Accordingly, there should be no reason in principle why an identical contract executed by different parties might in certain circumstances be given different interpretations.

- The Court of Appeal appears also to have overlooked a more cogent justification for the presumption where a financial institution is concerned. Rather than deriving from the financial strength and probity which is usually associated with financial institutions, the presumption is better said to flow from the fact that such institutions are in the business of issuing demand instruments for a fee without any involvement in the underlying transaction. Those are the circumstances which usually point strongly toward an on-demand instrument, as the prospect of such a financial institution wishing to become involved in a dispute about the merits of an underlying dispute is unrealistic and is very unlikely to have been intended. Bearing this in mind would also address the Court’s concern over the “non-binary” nature of whether an entity can be said to have a financing role or not. The more relevant question is whether the entity has issued the instrument for a fee in the course of a banking business, rather than as part of any commercial interest it may have in the underlying transaction.

In the short term, the Court of Appeal’s decision will inevitably lead to an increase in disputes over the interpretation of such guarantees. Parent companies may now find themselves subject to arguments that guarantees are on-demand due to a close analysis of their wording shorn of any presumption. Somewhat less likely, Banks may in appropriate circumstances seek to argue for a conditional interpretation of instruments which might otherwise have been thought to have been reliably “on-demand”. For the time being, parent companies especially should pay particular attention to the wording of guarantees given in relation to international projects.

References:

Esal (Commodities) Ltd v Oriental Credit Ltd [1985] 2 Lloyd’s Rep 546; *Siporex v Banque Indosuez* [1986] 2 Lloyd’s Rep 146; *Gold Coast Ltd v Caja de Ahorros* [2002] 1 Lloyd’s Rep 617; *Marubeni Hong Kong & South China Ltd v Ministry of Finance of Mongolia* [2005] EWCA Civ 395; *Vossloh AG v Alpha Trains (UK) Ltd* [2010] EWHC 2443 (Ch); *Wuhan Guoyu Logistics Group Co Ltd v Emporiki Bank of Greece SA* [2012] EWCA Civ 1629; *Shanghai Shipyard Co Ltd v Reignwood International Investment (Group) Company Ltd* [2020] EWHC 803 (Comm); *Shanghai Shipyard Co Ltd v Reignwood International Investment (Group) Company Limited* [2021] EWCA Civ 1147.

Challenging bond calls on international projects: English courts vs Emergency Arbitrators

A decision of the English Commercial Court last year has refused an application for an injunction requiring a beneficiary under an on-demand bond to withdraw its demand and refrain from making further demands pending the decision of an Emergency Arbitrator. The decision provides important guidance as to the relationship between Emergency Arbitration proceedings and interim relief from the English Courts. The decision also comments on the extent to which the approach of an Emergency Arbitrator may differ from that taken by the English courts when determining questions under a contract governed by English law.



Shapoorji Pallonji & Company Private Ltd v Yumn Ltd

Yumn Ltd (YL) appointed Shapoorji Pallonji and Company Private Ltd (SPC) (and some of its related group companies) to construct a power plant in Rwanda. The project agreements were based on the FIDIC form, were all subject to English law and provided for disputes to be resolved by ICC arbitration seated in Singapore.

SPC gave an on-demand performance bond in the sum of USD 32.2m. The bond, which was issued by Standard Bank, was subject to English law and the jurisdiction of English courts. Other than a prescribed form of demand and the requirement for demands to be delivered within business hours, the bond did not stipulate any other conditions precedent for a valid demand.

The original Date for Taking Over of the Works was 23 February 2020. Significant delays occurred for which SPC claimed extensions of time. YL refused to extend time on the basis that SPC had failed to notify its claims with the periods required by the contracts.

On 24 February 2021, YL made a written demand under the project agreements for payment of delay liquidated damages which, in the absence of an extension of time, had reached their maximum limit under the contracts. In the absence of payment, YL demanded the full amount of the performance bond from Standard Bank on 23 March 2021 citing, among other things, SPC's liability for delay liquidated damages.

Standard Bank informed SPC of the demand on 26 March 2021. SPC immediately requested that YL withdraw the demand and a sent solicitors' letter alleging that the demand was "*fabricated*". SPC also commenced two sets of proceedings seeking to prevent payment under the bond:

- ICC Emergency Arbitrator proceedings seeking orders against YL to suspend its demand against Standard Bank and prevent any further demands being made; and
- An application to the English Commercial Court under section 44 of the Arbitration Act 1996 for orders that YL withdraw its demand under the bond and refrain from making further demands pending the order of the ICC Emergency Arbitrator.

The Commercial Court delivered judgment swiftly, within 8 days of SPC's application and prior to any consideration of the matter by the Emergency Arbitrator.

Relief pending Emergency Arbitration

Although SPC maintained its position that YL's demand was fraudulent, its primary position before the Commercial Court was that the propriety of YL's demand was a matter for the Emergency Arbitrator and, thereafter to the extent necessary, a fully constituted arbitral panel under the ICC rules. SPC therefore submitted that the Commercial Court should grant orders preserving the *status quo* until the Emergency Arbitrator could decide on the issue. In support of this argument, SPC claimed that an Emergency Arbitrator was likely to adopt a less stringent approach than that taken under English law to the question of whether YL should be compelled to withdraw their demand and/or be restrained from making further demands.

For the purpose of this argument, the Court was content to assume that the propriety of YL's demand was caught by the arbitration agreement governing the project agreements. However, the Court considered it arguable that disputes as to YL's entitlement to make a demand under the bond might fall outside the arbitration agreement, given the inclusion with the bond of an English law and jurisdiction clause and the bond being in a form which was annexed to the project agreements.

The Court was also prepared to accept that an Emergency Arbitrator might arguably adopt a different approach to that adopted by the English courts. However, the Court noted that English law was the law governing both the project agreements and the performance bond and, accordingly, the fact that Singapore law (i.e. the curial law governing the arbitration proceedings) appeared to adopt a different approach to attempts to restrain the enforcement of bonds was immaterial. The Court also noted that whilst it was arguable that an ICC Emergency Arbitrator might apply procedural rules and principles that are different from and independent of those applied by an English court, that did not "*lead necessarily to the conclusion that the emergency arbitrator will grant the order sought by SPC when a court in England would not.*" The principles of substantive English law governing the enforcement of on-demand bonds would "*apply irrespective of whether the issues are being considered by a court in England or by an international arbitrator required to apply substantive English law to the dispute between the parties.*"

Having nevertheless assumed the above two matters in SPC's favour, the Court found it would not be appropriate to grant relief under section 44 merely to preserve the status quo pending the determination of SPC's application to the Emergency Arbitrator. The



Court considered that the same English law principles as to the enforcement of on-demand bonds should apply regardless of whether interim relief was sought in aid of an arbitration or generally in relation to court proceedings (under section 37 of the Senior Courts Act 1981). The Court also emphasised SPC's delay in commencing Emergency Arbitration proceedings. The dispute over extensions of time was longstanding and YL's formal demand for payment of delay liquidated damages had been issued a month prior to the demand under the bond. As the Court noted: *"It was open to SPC to refer the failure of YL to grant any of its applications for extensions in time to arbitration as soon as those applications had been refused and the contractual mechanisms for resolving such disputes had been exhausted and in that reference to seek an order from an EA from restraining YL from calling on the demand bond pending the resolution of that dispute. It chose not to do so."*

The English law principles

Having rejected SPC's primary position, the Court considered whether SPC was entitled to have YL withdraw its demand under English law. The Court noted there was little prior authority on the principles governing applications to require the withdrawal of demands, but guidance could be taken from cases dealing with other bond enforcement scenarios.

In relation to applications to restrain underwriters, such as the bank in this case, from complying with their obligations under an on-demand security, in the absence of a dispute as to the formal validity of the demand a Court would only grant an injunction where it is established that *"the only realistic inference is that (a) the beneficiary could not honestly have believed that it was entitled to make a demand for payment and (b) the bank was aware that the demand was fraudulent."*

In relation to applications to restrain a beneficiary, the Court noted that an injunction would generally only be granted to restrain a beneficiary from breaching an express or implied restriction contained in the underlying contract. In this case, however, there were no express conditions precedent to a demand and no implied obligations were asserted. Short of such restrictions, an application to restrain a beneficiary would need to satisfy the same test for fraud quoted above applicable to applications against underwriters. Provided these requirements were met, there was no reason why a beneficiary could not be forced to reverse the steps it has taken to enforce its rights under the instrument in question (i.e. through an order requiring the withdrawal of a demand).

In the present case, SPC had not come close to satisfying the fraud exception. It had not submitted any evidence to challenge YL's belief that SPC's failure to



comply with the notification requirements of the project agreements had invalidated its claims to extension of time. There was nothing to suggest the dispute was *“anything other than a delay dispute between an employer and contractor of the sort that arises on a regular basis in the civil engineering and construction sectors.”*

Conclusions and implications

Emergency Arbitrator proceedings are still a relatively new procedure in the arbitral world and guidance as to the relationship between such proceedings and interim relief from the English courts under section 44 of the Arbitration Act has been scant. This decision therefore provides valuable guidance as to the approach to be taken under section 44 where relief is sought in relation to calls under on-demand securities.

The Court’s refusal to play second-fiddle to Emergency Arbitration has considerable strategic implications for parties involved in such disputes. The arguments made by SPC suggest a perception that Emergency Arbitration provides a more lenient forum for Contractors wishing to challenge the enforcement of an on-demand security. The Court’s refusal merely to preserve the *status quo* pending Emergency Arbitration will encourage Contractors to pursue such proceedings at an earlier stage and in advance of a call being made if it all possible.

The Court’s comments as to the potential for Emergency Arbitrators to apply a more lenient approach are also of note. The comments are likely to be quoted in support of the application of English law principles by Emergency Arbitrators where English substantive law is applicable to the underlying contracts. On the other hand, the Court was concerned not to make a *“pre-emptive challenge”* to the decision of the Emergency Arbitrator and noted that *“he must be left to do his work as he considers appropriate”*.

Somewhat more significant is the Court’s suggestion that a general arbitration clause may not extend to disputes in relation to an on-demand bond where that bond has applicable law and jurisdiction clauses and its form is annexed to the underlying construction contract. This is a fact pattern which is likely to apply to a great many cases and beneficiaries may well seek to rely on these comments to resist Emergency Arbitration proceedings commenced by a Contractor.

Finally, the decision provides helpful confirmation as to the English law principles which apply where orders are sought against a beneficiary for the withdrawal of an existing demand – an area in which some uncertainty had previously existed.

References:

Shapoorji Pallonji & Company Private Ltd v Yumn Ltd [2021] EWHC 862 (Comm).

Liquidated damages and termination: orthodoxy restored

In the 2020 edition of this Annual Review, we reported on an English Court of Appeal decision which had suggested that for many construction contracts, including typically drafted FIDIC contracts, accrued liquidated damages amounts would fall away in the event of termination, leaving an employer with a general damage claim for delays arising before and after termination. This was thought to be a surprising decision by many commentators and has now been overturned by the UK Supreme Court. While ultimately the question will be one of interpretation of the clause in question, the Supreme Court has restored the “orthodox” position that the contractor should be liable for liquidated damages up to termination and thereafter general damages should apply. The Supreme Court also held that the term “negligence” in a limitation clause should be given its ordinary legal meaning of a breach of a contractual duty of care and concurrent duty of tort.



Termination and liquidated damages clauses

Whether a clause entitling an employer to claim liquidated damages for delay will survive termination has been decided inconsistently in previous cases. A House of Lords decision in 1912 (*British Glanzstoff Manufacturing v General Accident, Fire and Life Assurance Co*) decided that such a clause applied only where the original contractor completed the works and was not applicable upon termination. However, this decision appears to have been overlooked in the modern cases.

More recent cases have held that liquidated damages accrue up until the date of termination, but not thereafter. The employer is then left to bring a general claim for unliquidated damages for post-termination delays. Other recent cases have held that liquidated damages continue post-termination until the works are completed by the employer or a new contractor. The justification for this is said to be that any other approach would reward the contractor for its own default. This was the line taken most recently by the English Commercial Court in *GPP Big Field v Solar EPC Solutions*.

Triple Point Technology Inc v PTT Public Company Ltd

In this case, PTT entered into a contract for the procurement of software and related services from Triple Point. The contract documents provided for payment by milestones, but also included specific dates for payment. Work under the contract was delayed and Triple Point sought payment according to the dates referred to in the contract documents. PTT refused payment on the basis that the relevant milestones had not been achieved. Triple Point suspended work for non-payment and PTT purported to terminate the contract for Triple Point's default.

Among other issues in dispute, a question arose as to whether PTT could claim liquidated damages for delay. The liquidated damages clause at Article 5.3 of the contract provided:

"If CONTRACTOR fails to deliver work within the time specified ... CONTRACTOR shall be liable to pay the penalty at the rate of 0.1% (zero point one percent) of undelivered work per day of delay from the due date for delivery up to the date PTT accepts such work".

The English Technology and Construction Court (the TCC) held that PTT was entitled to liquidated damages up until the date of termination in respect of incomplete milestones.

The Court of Appeal

The Court of Appeal upheld Triple Point's appeal on this point and found that no liquidated damages accrued for incomplete milestones in circumstances of termination. Lord Justice Jackson set out the three inconsistent lines of authority identified above, noting that *British Glanzstoff* had not been cited in the modern cases despite it being *"a decision of our highest court, which has never been disapproved"*.

Although the outcome in each case depends on the precise wording of the clause in question, the Court of Appeal expressed doubts about the cases which permit liquidated damages for delay to persist beyond termination. This echoes criticism made by commentators in relation to these cases.

The Court also identified difficulties with the view, favoured by most textbooks, that liquidated damages apply up to the date of termination, but not beyond. Whilst this might be said to preserve accrued rights, it may be artificial to divide the employer's right to damages for delay into a period of liquidated damages prior to termination and a period of general damages after termination: *"It may be more logical and more consonant with the parties' bargain to assess the employer's total losses flowing from the abandonment or termination, applying the ordinary rules for assessing damages for breach of contract."*

The clause before the Court specifically referred to liquidated damages accruing *"up to the date PTT accepts such work"*. This was found to be similar to that considered in *British Glanzstoff* in that the completion of the work was expressly contemplated. Accordingly, the proper interpretation was that the entitlement to liquidated damages in respect of incomplete milestones fell away entirely upon termination and was replaced by a right to claim general damages for delay, subject to proof by PTT.

The Supreme Court

In overturning the Court of Appeal's judgment on this point, the Supreme Court held that the Court of Appeal erred in finding that the wording of Article 5.3 was sufficiently similar to that in *British Glanzstoff*. The liquidated damages clause in *British Glanzstoff*, was not market-accepted wording or a standard form clause and therefore could not be authority for any legal principle, even if the contractual wording in a later case was similar. The case was one which turned on its particular facts and did not establish any general proposition of law.

The Supreme Court went on to state that clear words would be required to overturn what is understood to be the “orthodox approach”, being that liquidated damages would be payable for delays up to termination, and thereafter the contractor would be liable in general damages for the employer’s termination losses. Indeed, Triple Point was unable to provide the Supreme Court with any examples of where standard form contracts expressly provided that liquidated damages for delay would only be payable if the contractor actually completes the work; the only example cited was clause 15.4(c) of the 2017 FIDIC Yellow Book which reflects the “orthodox” approach.

The Supreme Court dismissed the Court of Appeal’s concern that the orthodox approach might result in the employer finding itself in “new territory” with an “artificial” categorisation of the employer’s losses as being a specific amount per day or week up to a certain date and then general damages thereafter. Instead, it considered that it is established law that the accrual of liquidated damages comes to an end on termination of the contract, after which the parties must seek general damages for breach of contract.

The Court of Appeal’s approach was also criticised for being inconsistent with commercial reality and the accepted function of liquidated damages, i.e., that they benefit each of the employer (in avoiding the need to prove actual loss flowing from the delay) and the contractor (in providing certainty as to its liability in the event of its culpable delay). As such, and applying established rules of interpretation to Article 5.3, the Supreme Court considered that it could be fairly and reasonably interpreted as meaning “*up to the date (if any) PTT accepts such work*”.

Exclusion for “negligence”

By a slim majority, the Supreme Court also overturned the Court of Appeal’s ruling on a separate question as to the application of a cap on liability. The contract excluded from the cap liability resulting from “negligence” in the following terms:

*“This limitation of liability shall not apply to CONTRACTOR’s liability resulting from fraud, **negligence**, gross negligence or wilful misconduct of CONTRACTOR or any of its officers, employees or agents”*

The Court of Appeal had found that the reference to “negligence” here referred to a “free standing tort of negligence” that did not include breach of contractual duty of care or a concurrent duty of care in tort. As such, damages that arose due to the contractor’s negligent breach of contract fell within the cap on liability.

The Supreme Court disagreed. It held that the provisions should be interpreted in the context of the preceding sentences of exclusion clause, which expressly referred to “breaches of contract” and liability “under” the contract, and the scope of services and deliverables Triple Point had agreed to provide under the contract. Applying established rules for interpreting contracts, “negligence” in this clause should be given its accepted meaning in English law, i.e. incorporating both a breach of contractual duty of care and the tort of failure to use due care.

Conclusions and implications

The Supreme Court’s ruling will be welcomed by employers and contractors alike who benefit from the certainty that delay liquidated damages provide. The judgment is particularly notable for its application of established rules for interpreting contract provisions by applying, in so far as objectively possible, and in the context of the contract, words used in their ordinary sense.

The Court of Appeal’s decision had raised difficult issues for employers considering termination of a construction contract with the potential for accrued rights to delay liquidated damages being replaced with a general right to damages only and the attendant difficulties of proof that a general damages claim can give rise to. The Supreme Court’s decision sweeps away this difficulty and considerably simplifies this area of the law. Absent clear wording to the contrary, liquidated damages for delay accruing prior to termination will remain intact, with a general claim for damages applying only in relation to post-termination losses.

Parties may still wish to deal expressly in their contracts with how liquidated damages for delay will be applied in termination scenarios – particularly if something other than the “orthodox” position upheld in this case is intended. The Supreme Court’s decision also gives further encouragement, if any were needed, to pay close attention to how caps on liability (and any exclusions from them) are drafted.

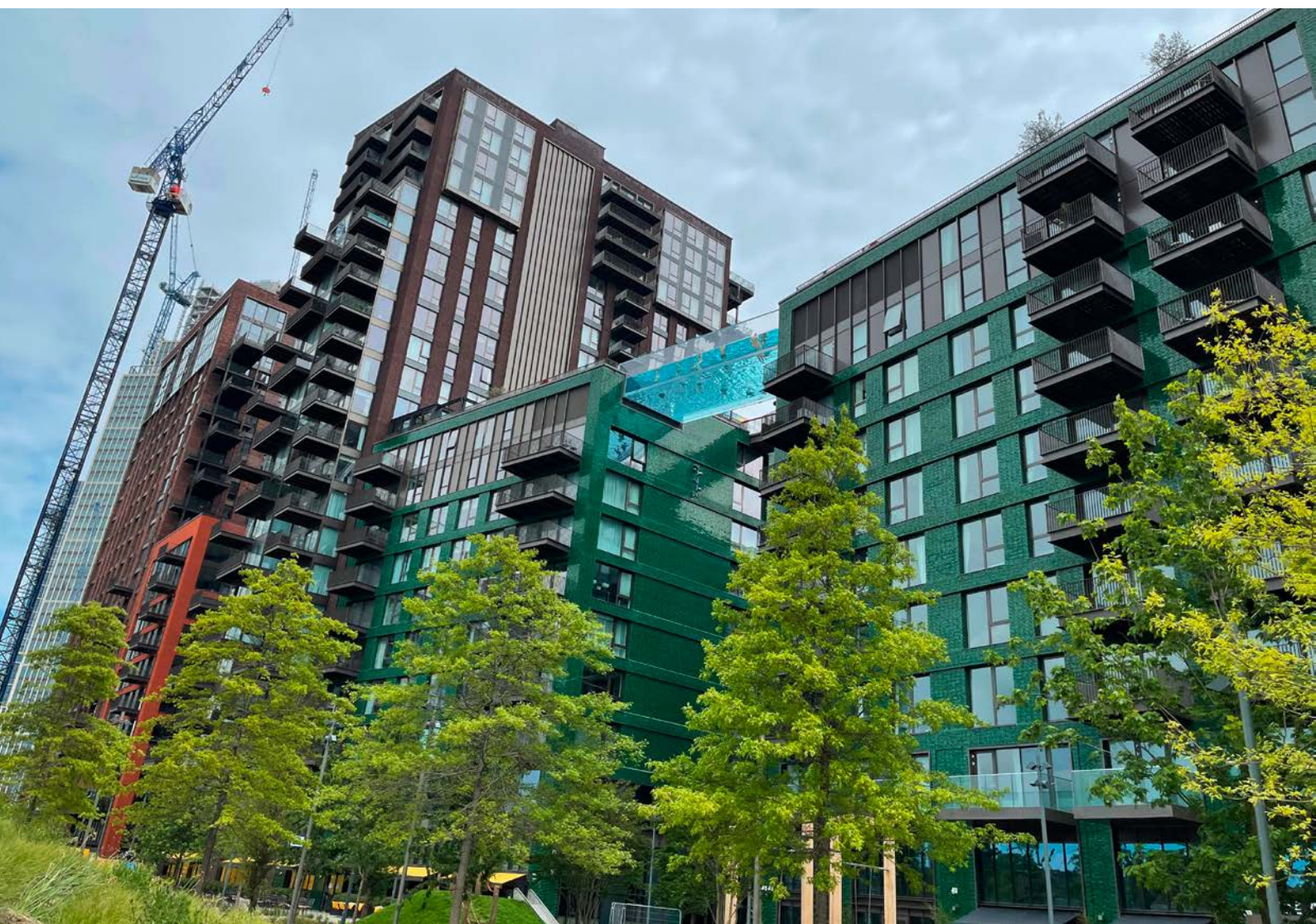
References:

British Glanzstoff Manufacturing Co Ltd v General Accident, Fire and Life Assurance Corpn Ltd [1913] AC 143; *GPP Big Field LLP v Solar EPC Solutions SL* [2018] EWHC 2866 (Comm); *Triple Point Technology, Inc v PTT Public Company Ltd* [2019] EWCA Civ 230; *Triple Point Technology, Inc v PTT Public Company Ltd* [2021] UKSC 29.



Liquidated damages and partial taking-over

An English Technology and Construction Court (TCC) decision last year has enforced a liquidated damages clause which did not allow for a proportionate reduction in liquidated damages following partial possession of completed sections of a project. The court rejected arguments that the clause was a penalty relying on principles established by the UK Supreme Court in the recent *Makdessi* case. The court also considered a number of alternative arguments of general interest, including whether the employer had an obligation to consider levying a reduced amount of liquidated damages and whether an otherwise invalid liquidated damages clause could nevertheless operate as a cap on liability.



Eco World – Ballymore Embassy Gardens Company Limited v Dobler UK Limited

Eco World engaged Dobler to carry out the design, supply and installation of façade and glazing works for a residential development in Nine Elms, London. Dobler were engaged on three parts of the development: Block A, comprising high value residential apartments and Blocks B and C, comprising affordable housing units. The contractual date for completion was 30 April 2018. On 15 June 2018, Eco World took over Blocks B and C. On 20 December 2018 all of Dobler's works were certified as achieving practical completion.

Following practical completion, a dispute arose as to the level of liquidated damages Eco World were entitled to for Dobler's delay. After an initial grace period after the Date for Completion, the contract provided for a single weekly sum as follows:

"Liquidated damages will apply thereafter at the rate of GBP 25,000 per week (or pro rata for part of a week) up to an aggregate maximum of 7% of the final Trade Contract Sum..."

The contract also contained equivalent provisions to those contained in the JCT suite of contracts which required Eco World to notify that it required Dobler to pay liquidated damages at the rate stated in the contract *"or lesser rate stated in the notice"*.

Following a number of adjudications Eco World commenced proceedings in the TCC seeking declarations as to (1) the validity and/or enforceability of liquidated damages in circumstances where Eco World had taken possession of Blocks B and C and there was no mechanism for a proportionate reduction in the amount of the damages, and (2) if the clause was void, whether it nonetheless imposed a cap on the level of general damages Eco World were entitled to claim for delay.

Did partial possession make the liquidated damages clause unenforceable?

The TCC determined that the liquidated damages provision was valid and enforceable. Whilst the provision did not provide for a reduction in liquidated damages on partial possession, there was no uncertainty as to the amounts payable. The full amount of liquidated damages was payable for each week of delay regardless of any partial possession taken by Eco World.

The court then considered whether such a clause offended the rule against penalties laid down most recently by the UK Supreme Court in the *Makdessi* case. That required the court to consider whether the clause was *"extravagant, exorbitant or unconscionable"* and whether it was *"out of all proportion to"* to Eco World's legitimate interest in securing timely completion of the Works. Applying this test, the court determined that the provision did not amount to a penalty for the following reasons:

- The clause was negotiated by commercial parties and their lawyers and enabled each party to better manage the risk of delay in the completion of the project.
- Eco World had an interest in enforcing completion of the works as a whole by the contractual completion date as late completion would have an adverse impact on the rest of the project by delaying following trades, exposing Eco World to liability and put at risk prospective sales of the apartments.
- Alternative quantification of Eco World's damages would be difficult, particularly following partial possession. Different combinations of partially incomplete blocks could result in a wide range of loss scenarios. Stipulating a single rate for all scenarios avoided these complexities.
- No evidence had been submitted to suggest that the level of liquidated damages agreed was unreasonable or disproportionate to the likely losses in the event of late completion to any one or more of the blocks.

Did Eco World have an obligation to reduce the rate of liquidated damages?

Dobler also contended there was a contractual mechanism for reducing the level of liquidated damages payable. They relied on the standard JCT wording noted above, which allowed Eco World to stipulate a *"lesser rate"* of liquidated damages. Dobler claimed this language conferred a discretion on Eco World as to the amount of liquidated damages to be levied and that this discretion was required to be exercised reasonably and not in a capricious or irrational manner. It claimed that Eco World could not reasonably insist on the full amount of liquidated damages in circumstances where it had taken partial possession of Blocks B and C.

The Court rejected these contentions, finding that the ability of Eco World to levy a reduced amount of liquidated damages was an absolute contractual right, not one conferring a discretion with implied limitations.

Did the liquidated damages clause set a cap on liability even if penal?

Dobler also argued that if the liquidated damages clause was found to be penal/unenforceable then general damages should be capped at the level of liquidated damages otherwise payable. The court agreed. Despite *Makdessi* providing support for the view that general damages should not be limited to the amount of any penalty found to be unenforceable, the court considered the clause in this case had two parts; firstly containing a weekly rate for liquidated damages but also stipulating an overall cap on liability for delay. Were the rate of liquidated damages to be struck down due to the rule against penalties, the overall cap on liability could nonetheless be given effect to.

Conclusions and implications

This decision provides an interesting insight into how the court's approach to penalty arguments has changed in light of the *Makdessi* decision. Dobler had relied on extracts from leading construction texts *Keating* and *Hudson* expressing the view that the absence of a mechanism for reducing liquidated damages on account of partial possession would cause a claim for liquidated damages to fail. However, the court's analysis shows there are good reasons why a single liquidated damages sum might be agreed despite (and precisely because of) the prospect of many different partial possession scenarios. It was not sufficient for Dobler simply to show that the same amount liquidated damages would be payable in partial possession scenarios where Eco World's loss would be much lower than without partial possession. Dobler needed to go further and show that the liquidated damages agreed on were out of all proportion to Eco World's legitimate interest in securing timely completion of the works.

Given the greater breadth of this new test, it is surprising that Dobler did not seek to lead evidence as to the actual losses Eco World would suffer in particular scenarios nor as to the likelihood of partial possession when the contract was entered into. Had it been favourable, such evidence may have lent greater weight to Dobler's arguments, although it is plain from the judgment that such evidence would need to have been sufficiently strong to characterise the liquidated damages agreed upon as being "*extravagant, exorbitant or unconscionable*".

Other similar cases dealing with the enforceability of liquidated damages provisions in partial possession scenarios have been decided differently, because the drafting of the relevant provisions were void for uncertainty. This reiterates the importance of clearly and unequivocally reflecting the parties' intentions when drafting. If the contract allows for partial possession and the parties intend for liquidated damages to be reduced accordingly, the contract must state that. It must also be clear what the relevant reduction will be and/or provide a mechanism for determining that reduction.

References:

Cavendish Square Holding BV v Talal El Makdessi [2015] UKSC 67; *Eco World – Ballymore Embassy Gardens Company Limited v Dobler UK Limited* [2021] EWHC 2207 (TCC).





“No oral modification” clauses: an international divide

A recent decision of a five-judge Court of Appeal in Singapore has considered the legal effect of no oral modification clauses (NOM clauses) under Singaporean law. In a break with the position in the UK (decided in the *Rock Advertising* case), the Court held that NOM clauses merely raise a rebuttable presumption that in the absence of an agreement in writing, there would be no variation. Under the strict approach adopted in *Rock Advertising*, NOM clauses are given full effect such that any subsequent modification to the contract will be invalid unless it complies with the formalities stipulated in the NOM clause. The Court also suggested that a more liberal approach to estoppel would apply than indicated in *Rock Advertising* were a NOM clause to result in the invalidity of an oral agreement. Given the prevalence of such clauses in commercial contracts, this divergence between the English and Singaporean law may have a significant impact on governing law choices going forward.



Introduction

Large international construction contracts are typically administered for employers and contractors alike by project managers or engineers within defined project teams. In a FIDIC context, these positions are occupied by the Engineer and the Contractor's Representative (and any of their delegates or assistants). Throughout the course of a project, these personnel will discuss a broad range of issues, including technical matters, financial details and the legal merits of particular positions adopted by either party. As they are appointed by the parties and given responsibility for the management of such issues, these personnel will usually have authority to conclude agreements on behalf of the parties or to make statements which have legal effect under the relevant construction contract. Given that project level discussions often take place informally, risks arise that agreements or statements may be made without proper consideration or without prior approval of senior management. So called "no oral modification clauses" ("NOM clauses" for short) and "no-waiver" clauses are often included within construction contracts to protect against these risks.

NOM clauses will typically seek to preclude the making of variations or amendments to a contract unless certain formalities are followed. A popular form is to require that any amendment be "in writing and signed by the parties". "No-waiver" clauses are similar and will usually seek to preclude informal waivers of rights by stating that any waiver must be in writing and signed by the party concerned. In a construction context, NOM clauses are often drafted to preclude payment for varied or additional work unless agreed or instructed in writing by the employer or the employer's engineer or architect.

The effectiveness of these clauses has long been questioned on the basis that freedom of contract requires that parties be able to make new contracts through whatever means they choose and they cannot therefore put beyond their power their ability to do so in the future. Others argue that by giving effect to them the courts are upholding an exercise of the parties' freedom of contract. Under English law this debate was decisively determined in favour of upholding such clauses by the UK Supreme Court in *Rock Advertising Ltd v MWB Business Exchange Centres Ltd* decided in 2018.

Rock Advertising: a recap

Rock Advertising involved a licence agreement for office space for a fixed term of 12 months. The licence contained a NOM clause in the following terms: "All variations to this Licence must be agreed, set out in writing and signed on behalf of both parties before they take effect."

Six months later, the director of the licensee (Rock Advertising) had a telephone conversation with a credit controller from the licensor (MWB) about payment arrears. The court at first instance found that, during this conversation, a variation to the payment schedule was agreed. However, MWB treated the variation as merely a proposal and ultimately rejected the varied schedule. It then proceeded to lock Rock Advertising out of the premises for failure to pay the arrears and terminated the licence.

The Supreme Court upheld MWB's position, finding that the NOM clause was effective against the oral agreement relied on by Rock Advertising. The Court disagreed that the making of such an oral agreement implicitly dispensed with the NOM clause:

"What the parties to such a clause have agreed is not that oral variations are forbidden, but that they will be invalid. The mere fact of agreeing to an oral variation is not therefore a contravention of the clause. It is simply the situation to which the clause applies. ... The natural inference from the parties' failure to observe the formal requirements of a No Oral Modification clause is not that they intended to dispense with it but that they overlooked it. If, on the other hand, they had it in mind, then they were courting invalidity with their eyes open."

The Court also considered the potential for injustice to arise where oral agreements in contravention of an anti-variation clause have been acted upon by the parties who then find themselves unable to enforce the agreement. The Court left open whether the doctrine of estoppel might assist a party in such circumstances, although at the same time identifying a number of difficulties lying in the path of such an argument:

"In England, the safeguard against injustice lies in the various doctrines of estoppel. This is not the place to explore the circumstances in which a person can be estopped from relying on a contractual provision laying down conditions for the formal validity of a variation. The courts below rightly held that the minimal steps taken by Rock Advertising were not enough to support any estoppel defences. I would merely point out that the scope of estoppel cannot be so broad as to destroy the whole advantage of certainty for which the parties stipulated when they agreed upon terms including the No Oral Modification clause. At the very least, (i) there would have to be some words or conduct unequivocally representing that the variation was valid notwithstanding its informality; and (ii) something more would be required for this purpose than the informal promise itself ..."

Charles Lim Teng Siang v Hong Choon Hau

A full panel of Singapore's highest court has now decided not to follow the reasoning of the UK Supreme Court in *Rock Advertising*. In this case, Mr Lim and others (the Sellers), entered into a sale and purchase agreement (SPA) with Mr Hong and Mr Tan (the Buyers), pursuant to which the Sellers were to sell 35m shares in a public listed company to the Buyers for SUSD 10.5m.

The SPA provided for a completion date of 17 October 2014 (Completion Date) and that time would be of the essence. It also contained an NOM clause which provided that "*No variation, supplement, deletion or replacement of any term of the SPA shall be effective unless made in writing and signed by or on behalf of each party*" (SPA NOM Clause).

Over 3 years had passed after the Completion Date before the Sellers' solicitors issued a letter to the Buyers, demanding compliance with the SPA and threatening legal action. The Sellers subsequently commenced action in the High Court of Singapore, claiming damages for breach of the SPA due to the Buyer's failure to complete.

The Buyers denied being in breach of the SPA and amongst other things, claimed that pursuant to an alleged telephone call between Mr Lim and Mr Hong on or about 31 October 2014, the SPA was rescinded by mutual agreement. The High Court accepted the Buyer's evidence in this regard and rejected the Seller's claim.

On appeal to the Court of Appeal of Singapore, the Sellers raised, among other things, a new argument that the alleged oral rescission, even if proved, was invalid because the requirements of the SPA NOM Clause had not been satisfied. The Buyers argued that the SPA NOM Clause did not apply to rescission and could not in any event invalidate an oral agreement contrary to its terms which had been adequately proved.

NOM clause not applicable to rescission agreements

The Court held that based on its plain language, the SPA NOM Clause did not apply to the rescission of the SPA as it only expressly provided that a "variation, supplement, deletion and replacement" must be made in writing. The common denominator underlying these four forms of modifications is that the SPA will continue to remain valid and in force, which is in contrast to the effect of a rescission. The appellants' arguments that a rescission amounted to "replacing" the SPA with an agreement to rescind, or that it "deleted" the clauses in

the SPA which required performance of the share transaction, and that such deletion led to the rescission of the SPA, were rejected by the Court.

On the facts, the Court agreed with the High Court of Singapore that the parties had orally agreed to rescind the SPA via the telephone call on 31 October 2014.

The legal effect of NOM clauses

Even though it was not strictly necessary to do so, the Court also proceeded to discuss and clarify the legal effect of NOM clauses in general.

The Court examined the current schools of thought in this regard by reference to law from other jurisdictions:

- First, the strict approach taken by the majority of the UK Supreme Court in *Rock Advertising* (delivered by Lord Sumption). Under this approach, any subsequent modification to the contract must comply with the formalities stated in the NOM clause, otherwise it will be deemed invalid. As such, an NOM clause can only be removed by an agreement of the parties which complies with the formalities set out in the NOM clause.
- Second, the approach developed by Lord Briggs in *Rock Advertising*. Under this approach, the parties' oral agreement specifically to depart from an NOM clause will be treated as valid. Such oral agreement may be express or by necessary implication. However, in situations where an oral variation is made without express reference to the NOM clause, a strict test should be applied before the court finds that parties had, by necessary implication, agreed to depart from the NOM clause.
- Third, the approach endorsed by the Singapore Court of Appeal in *Comfort Management Pte Ltd v OGSP Engineering Pte Ltd*. Under this approach, an NOM clause merely raises a rebuttable presumption that in the absence of an agreement in writing, there would be no variation. Incidentally, this approach was adopted from the English Court of Appeal's decision in *Rock Advertising* which was later reversed by the UK Supreme Court on appeal.

The Court confirmed the third approach, siding with the Court of Appeal in *Rock Advertising* and disagreeing with the two Supreme Court approaches. Underlying this difference is the emphasis the respective courts placed on parties' intentions at the time of entering into a contract. Lord Sumption's view in *Rock Advertising* was to the effect that once parties had agreed to regulate their legal relations, then they are bound by



those regulations. Each party's autonomy operates up to the point when the contract is made, but thereafter only to the extent that the contract allows.

On the other hand, the Court took the view that fixing the parties' intention at the time the contract was entered into overlooks the fact that parties to a contract had the autonomy to change the terms of the contract. In the Court's opinion, Lord Sumption's view conflated the parties' individual autonomy (which should necessarily be bound by the terms of the contract) with the parties' collective autonomy. Collectively, the parties to a contract should be able to jointly agree to vary any aspect of their own agreement and the court should uphold their autonomy to do so.

While the Court recognised there are several legitimate commercial reasons why parties may choose to include NOM clauses in their contract, those reasons do not provide a legitimate basis to prevent parties from varying a contract orally where such an oral variation can be proved. The Court distinguished between proving the fact that an oral variation had taken place (and the evidential difficulties that come with it) and recognising an oral variation at all in cases where there are NOM clauses.

Nevertheless, the Court emphasised that compelling and cogent evidence is required before the court will find and give effect to an oral variation in order to rebut the presumption that there is no oral variation. This does not modify the standard of proof, but rather *"serves to reflect the inherent difficulty in proving such an oral variation in the face of their express agreement to the contrary as prescribed in the NOM clause."* However, this perceived evidential difficulty in proving the oral variation should not be confused or conflated with the question of the legal effect of a NOM clause.

Once the burden of proof in relation to the oral variation is discharged, the NOM clause will cease to have legal effect because such is the collective decision of both parties to the contract. The test, according to the Court, should be whether at the point when parties agreed on the oral variation, they would necessarily have agreed to depart from the NOM clause had they addressed their mind to the question, regardless of whether they had actually considered the question or not.

Although, strictly speaking, the Court's decision on these points is obiter, and therefore not binding, the fact that the decision was made by a panel of five judges of Singapore's highest court means that it is very likely to be followed in future cases.

NOM clauses and estoppel

For completeness, the Court also observed that even where NOM clauses to have the strict effect found by the UK Supreme Court, the doctrine of equitable estoppel would nevertheless be likely to apply in most cases where an oral agreement had been proved. This was because in most cases such an agreement is likely to be provided by the parties' subsequent conduct in performing the contract as orally varied. Accordingly, *"in most circumstances where an oral variation (which would in itself constitute a clear and unequivocal representation) is proved, the parties should be able to establish detrimental reliance on the oral variation (the act of performing the obligations of the oral variation), and thereby satisfy the doctrine of equitable estoppel."*

This finding contrasts with a stricter approach to such estoppels indicated by Lord Sumption in *Rock Advertising* and subsequently applied by the English courts. The English approach requires more than mere reliance on an oral promise; some statement or conduct is needed which unequivocally represents that the oral variation was valid notwithstanding its non-compliance with the NOM clause.

Consequences and wider application

As noted in the introduction, NOM clauses are prevalent in commercial contracts, included to ensure commercial and legal certainty, and to prevent costly disputes as to the proof or disproof of alleged oral modifications. In these circumstances, a party to a contract governed by Singapore law seeking to rely on an NOM clause should ensure that any oral discussions that may have the effect of, and/or be relied upon as, modifying the terms of the underlying contract be properly clarified as not being binding unless documented in accordance with the formalities set out in the NOM clause.

In circumstances where parties are seeking to rely on such oral discussions, the safest approach is still to comply with the NOM clause, but if that is not practical then proper notes and records should be taken. As stated by the Court of Appeal, compelling and cogent evidence is required in order to make a finding that there has been an oral agreement to modify the terms of the contract.

Further, clear policies and guidelines should be established in respect of the day-to-day management and execution of the contract so that daily discussions or off the record conversations do not have the unintended effect of modifying the terms of the contract. Where there has been some form of discussion

or communication that has the effect of modifying the terms of the contract, a party that has allowed the other party to rely on this discussion or communication to its detriment could also be estopped from relying on the NOM clause.

The Court's decision may also have relevance to the continued development of English law in relation to NOM clauses. While the UK Supreme Court's decision in *Rock Advertising* has authoritatively determined the English position in relation to the legal effect of such clauses, the position in relation to estoppel was addressed only in qualified *obiter* comments. The Court's suggestion in the present case that a more liberal approach might apply than indicated by Lord Sumption could therefore prove relevant in future English law cases.

As NOM clauses appear in many international model forms, the decision of the Court is of wide relevance across a variety of sectors. For example:

- The AIPN Model Form Operating Agreement (2012) requires an amendment to be a "*written amendment*" and "*signed*".
- Clause 74.5 of the BP Oil International Limited General Terms & Conditions for Sales and Purchases of Crude Oil and Oil Products (2015) also require modifications to be "*evidenced in writing*".
- Clause 34.8 of the LOGIC General Conditions of Contract for Construction, Edition 3 (2018) requires amendments to be "*evidenced in writing and signed by the PARTIES*".
- The NEC suite of contracts requires amendments to be "*in writing and signed by the parties*".

The Court's decision is likely also to be of great relevance if and when the courts of other common law countries come to reconsider the enforcement of NOM clauses. As noted in *Rock Advertising*, the majority of these jurisdictions – including the United States, Australia and Canada – do not strictly enforce NOM clauses. Whether in the future they will side with the UK Supreme Court or the Singapore Court of Appeal remains to be seen.

On a practical front, it should also be remembered that an email, in some jurisdictions, may be 'in writing' for the purposes of a NOM clause. For example, in *C&S Associates UK Ltd v Enterprise Insurance Company plc*, the English Commercial Court decided that:

- An exchange of emails was "*in writing*" for the purposes of a NOM clause.
- An email with a signature block was able to satisfy the requirement for an agreement to be "*signed*".

Finally, the wider implication of this divergence between English and Singaporean law (as well as the laws of other jurisdictions) on parties' choice of governing law should not be understated, particularly on multinationals and international parties conducting business globally. When considering alternatives in governing laws, parties should have a proper appreciation of the legal effect of NOM clauses.

References:

C&S Associates UK Ltd v Enterprise Insurance Company plc [2015] EWHC 3757 (Comm); *Rock Advertising Limited v MWB Business Exchange Centres Limited* [2018] 4 All ER 21; *Comfort Management Pte Ltd v OGSP Engineering Pte Ltd* [2018] 1 SLR 979; *Charles Lim Teng Siang v Hong Choon Hau* [2021] SGCA 43.

Negotiating agreements and endeavours clauses

Endeavours clauses are widely used in international construction contracts, including in various places within the FIDIC forms. They are often used to give “teeth” to an obligation for the parties to negotiate and agree on certain matters. Pure “agreements to agree” are unenforceable under English law and the addition of an endeavours obligation can be seen as a route towards enforceability. That is often not the case, as even the strongest of endeavours obligations will not be able to overcome any uncertainty inherent in the matters which are to be agreed upon. Where the object of the desired agreement is clear and well-defined, however, an endeavours obligation may permit an enforceable obligation to be drafted. An English case decided last year provides a good example of this approach in practice which successfully bound the parties to the negotiation of a further agreement.



Endeavours clauses

Endeavours clauses raise a number of issues of interpretation:

- What is the standard of “endeavour” required? Does “best endeavours” refer to every means available, or only those which are reasonable?
- What if there is more than one endeavour available which meets the standard? Should they all be pursued, or only one?
- Do such clauses require endeavours to be pursued even though they conflict with one’s own commercial interests?

The answer to the first issue is largely clear: the endeavours required are to be reasonable, even in the case of “best endeavours” clauses. One is not required to “move heaven and earth”. What will be reasonable in any given case depends on all the circumstances, including the nature of the contract and businesses involved and the financial position of the company upon which the obligation rests.

Given this position, one might well ask whether there is any difference between “reasonable endeavours” and “best endeavours”. This question was considered in *Rhodia International Holdings Ltd v Huntsman International*, where the difference was held to lie in the number of endeavours required to be pursued. “Reasonable endeavours” required only one of a number of reasonable endeavours to be pursued, whereas “best endeavours” required all reasonable endeavours to be pursued. In this context, the court noted that: “it may well be that an obligation to use all reasonable endeavours equates with using best endeavours”.

A “best endeavours” obligation may also be said to more readily require a party to subordinate its own financial interests to the agreed object. For example, in *Jet2.com v Blackpool Airport*, a contract between budget airline Jet2.com and Blackpool Airport (BAL) contained an agreement that both parties would “... co-operate together and use their best endeavours to promote Jet2.com’s low cost services”. This clause was held by the Court of Appeal to require BAL to allow Jet2 to operate outside of normal hours even if this required BAL to incur a loss as a result.

By contrast, a “reasonable endeavours” obligation will rarely require a party to sacrifice its own commercial interests. For example, in *Phillips Petroleum Company United Kingdom v Enron Europe*, a contract for the supply of North Sea gas contained a requirement for the

parties to use reasonable endeavours to agree the date on which deliveries of gas were to begin (a long-stop date was also specified in the absence of agreement). Because of a fall in the price of gas Phillips refused to agree a date earlier than the specified long-stop date. Enron argued that each party was under a duty to use reasonable endeavours having regard only to criteria of technical and operational practicability and without regard to selfish or commercial motives. The Court of Appeal disagreed, with Kennedy LJ finding it “impossible to say that [the contract terms] impose on the buyer a contractual obligation to disregard the financial effect on him, and indeed everything else other than technical or operational practicality ...”.

Similar reasoning was applied to an “all reasonable endeavours” clause in *CPC Group v Qatari Diar REIC* to conclude that, “the obligation to use ‘all reasonable endeavours’ does not always require the obligor to sacrifice his commercial interests.”

In practice, however, the extent to which any of these obligation will require significant expense to be incurred or commercial interests to be subordinated will be heavily dependent on the contractual context in which they appear. Thus, an important part of the reasoning in the *Jet2* decision was that the ability to operate out of hours was held to be essential to the airline’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 opening 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.”

Negotiating agreements

Bare agreements to negotiate, or “agreements to agree” as they are sometimes called, have long been held to be unenforceable under English law for the reason that they lack sufficient certainty. The same rule applies to agreements to use reasonable or best endeavours to negotiate an agreement. For example in *Multiplex Constructions UK Ltd v Cleveland Bridge UK Ltd* an agreement to “use reasonable endeavours to agree to re-programme the completion of the subcontract works and to agree a fixed lump sum and/or reimbursable subcontract sum for the completion of subcontract works” was found to be too uncertain to be enforced. As explained by the Court of Appeal in *Phillips Petroleum Co UK v Enron Europe Ltd*:

"The unwillingness of the courts to give binding force to an obligation to use 'reasonable endeavours' to agree seems to me to be sensibly based on the difficulty of policing such an obligation, in the sense of drawing the line between what is to be regarded as reasonable or unreasonable in an area where the parties may legitimately have differing views or interests, but have not provided for any criteria on the basis of which a third party can assess or adjudicate the matter in the event of dispute. In the face of such difficulty, the Court does not give a remedy to a party who may with justification assert 'well, whatever the criteria are, there must have been a breach in this case'. It denies the remedy altogether on the basis of the unenforceability in principle of an obligation which may fall to be applied across a wide spectrum of arguable circumstances."

Attempts have been made to overcome this rule by more closely defining the nature of the agreement which the parties must endeavour to secure and thereby reduce the level of uncertainty over the meaning and scope of the obligation. A good example of such an attempt, albeit which failed, is *Dany Lions v Bristol Cars*.

Dany Lions entered into a contract with Bristol Cars, a mechanic, for the restoration of a classic car. Bristol Cars entered administration during the contract and Dany Lions became concerned about the lack of progress. Bristol Cars suggested that Jim Stokes Workshops (JSW) be appointed to undertake the restoration works and this led to a Settlement Agreement being entered into on 4 May 2012 between Bristol Cars and Dany Lions. The Settlement Agreement was subject to a condition precedent that Dany Lions would enter an agreement with JSW, on or before 30 May 2012, to carry out restoration work to the car. Specifically, it stated:

"1.5 "Condition Precedent" means Dany Lions entering into an agreement with JSW on or before 30 May to carry out the works

2 Dany Lions will use its reasonable endeavours to fulfil the Condition Precedent."

Annexed to the Settlement Agreement was an email setting out the scope of the Works to be undertaken by JSW. The date for the Condition Precedent was extended to 19 January 2013 by agreement of the parties.

Dany Lions and JSW could not reach an agreement on the price of the restoration works. JSW proposed a figure of GBP 195,000 but this was considered to be unaffordable by Dany Lions (the original contract with Bristol Cars was a fixed price agreement for GBP 127,500).

A meeting was fixed for 17 January 2013 between Dany Lions, Bristol Cars and JSW. At this point JSW advised they were not willing to enter any fixed price contract as there were too many unknowns and they were concerned the true costs might be significantly higher than GBP 195,000. At this point, Dany Lions decided that it had used "reasonable endeavours" to fulfil the condition precedent and stopped negotiations with JSW (2 days before expiry of the date for the condition precedent).

Dany Lions proceeded to sue Bristol Cars for damages for non-performance of its obligations and claimed the difference between the fixed price under the original agreement and the actual cost of having the work carried out (which Dany Lions had now agreed directly with JSW under a new contract based on hourly rates). The key issue was therefore whether Clause 2 was enforceable.

The court noted there was a distinction to be drawn between a clause whose content was so uncertain that it was incapable of giving rise to a binding obligation, and a clause which gave rise to a binding obligation, the precise limits of which would be difficult to define in advance. In determining whether a contractual obligation to use best or reasonable endeavours is enforceable the initial focus is to be on the object of the endeavours clause. If the object of the clause is sufficiently certain, a court is able to know what it is that the party concerned must use his reasonable endeavours to achieve. However, even in a case where there is certainty as to the object there is still potentially a problem as to whether there are sufficient objective criteria by which to evaluate the reasonableness of the endeavours (i.e. the "yardstick" by which to measure the endeavours).

The court noted that the second problem of an appropriate "yardstick" was more likely to arise where the best endeavours obligations is directed at a future agreement between the parties. Even if the proposed agreement has clearly been set out in draft, so that the object of the endeavours obligation is clear, the court would lack any objective criteria against which to judge either party's refusal to agree. The position was said to be different if the same endeavours clause was directed at reaching agreement with a third party on terms which had already been identified. In such a case, the court would only be required to judge whether the endeavours made by one of the parties to procure the third party's agreement were sufficient.

On the facts, however, the court found that although the condition precedent required agreement with a third party (JSW), the object of the clause was too uncertain to be enforced. In particular, whilst the scope of work

was adequately defined, no reference was made to the cost of the work or the timing of payments. These were matters which the condition precedent envisaged being open to future negotiation between Dany Lions and JSW, and there were no objective criteria by which the court could evaluate whether it was reasonable or unreasonable for Dany Lions to refuse to agree to any particular terms on offer.

The court reached this conclusion with some regret noting that the condition precedent was clearly intended by the parties to form a binding and enforceable obligation. However, despite the parties' intentions, they had not provided a sufficient degree of certainty. In the absence of something said expressly as to the terms of payment, the court was unable to imply an obligation on Dany Lions to contract with JSW on reasonable market rates or anything similar.

Brooke Homes (Bicester) Limited v Portfolio Property Partners Limited

A more recent decision last year provides a rare example of an agreement requiring all reasonable endeavours to reach agreement being upheld by an English court. The case arose out of the proposed development of land to the North-West of Bicester, in Oxfordshire, designated for the building of a zero-carbon "eco-town". Between 2009 and 2014, two companies within the "P3 Group" built up a portfolio of land for development and, on 31 December 2014, they submitted an application for outline planning permission. Having started the planning process, the P3 companies set about finding a developer for the project. The claimant (Brooke) was identified as a suitable option due to its experience in modular housing which was compatible with the eco-town concept. The parties broadly agreed that, subject to the grant of planning permission and certain other conditions, Brooke would purchase land from the P3 companies' portfolio for the development of private residential homes. In April 2015 the parties formalised this intention by entering into Heads of Agreement and two associated contracts (the "Agreements"). Under the Agreements, the parties agreed to enter into a conditional sale agreement (CSA) for the purchase of an initial 100 acres of land subject to two conditions which were subsequently fulfilled. Further conditions were stated for the purchase of a further 400 acres thereafter. Details as to the timing and price for the initial 100 acres were recorded, but the exact location of the 100 acres was to be agreed from the land held by the P3 companies.

The Agreements required the parties to act in good faith and an exclusivity period was agreed during which the P3 companies would not negotiate for the sale of

the land with any third parties. The parties also committed to concluding a final binding agreement in the following terms:

"The parties shall use all reasonable endeavours to enter into a final binding Agreement which captures legally these Heads of Agreement acting in good faith towards each other ..."

The Agreements also recorded that:

"The transaction will be structured in a manner which will most effectively achieve the desired commercial and financial outcome for both parties."

Despite the grant of outline planning permission for the wider scheme in March 2017, the parties had failed to conclude the CSA and relationships had become strained. Brooke issued proceedings against the P3 companies in December 2018 complaining that they were in breach of contract for the sale of land to Brooke.

The court held that the P3 companies were in breach of their positive obligations under the Agreements to use all reasonable endeavours and to negotiate in good faith to translate the intended transaction into a CSA, depriving Brooke of the chance to secure a CSA on beneficial terms. The loss of chance was valued at GBP 13.4m and damages were awarded for this amount.

In reaching its decision, the court discussed the recognised differences between the different types of endeavours clauses (as noted above) and added the following comments in relation to an "all reasonable endeavours" clauses:

"active endeavour is required on the part of the parties where all reasonable endeavours are required: passivity or inactivity is likely to be construed as a potential breach. And if a reasonable course is identified by the claimant then the defendant can be required to explain why it was not required to do so."

One of the key factors in finding that the P3 companies had breached their obligations was the lack of a plan showing which initial 100 acre parcel of land would be sold to Brooke. The court was unpersuaded that a plan could not be produced (and, thus the CSA could not be concluded) because, until planning consent was granted, the P3 Group did not know exactly what land within the wider scheme was going to be permitted for private residential development. This was not an insurmountable problem, in the court's view, as the introduction of a clause which contemplated provisional demarcation of the land to be transferred was a reasonable alternative solution which the P3 companies failed to take forward.

The court noted that it might have been argued by the P3 companies that the endeavours obligation was an unenforceable agreement to agree – given that its object was a new agreement. The judgment records that this was not an argument that was advanced by the P3 companies. In this regard, the court surmised that:

*“No doubt they had in mind, when making that concession, the [principle] ... that in commercial dealings where the parties have acted in the belief that they had a binding contract, the courts are willing to imply terms, where that is possible, to enable the contract to be carried out. The courts will assist the parties to preserve rather than destroy bargains, on the basis that what can be made certain is itself certain. ... Cases such as *Petromec Inc v Petroleo Brasileiro SA Petrobras* ... show that the courts will now be willing to recognise an obligation to negotiate on some matter using reasonable endeavours, or in good faith, where it is found in a binding agreement.”*

The *Petromec* case concerned (in this respect) an express obligation to pay the reasonable extra costs and to allow extra time in relation to certain changes to an upgrade specification for a marine vessel. The parties also agreed to “negotiate in good faith ... the extra costs ... and the extra time ... and upon the determination of the same ... agree to enter into one or more addendums to this Agreement specifying the amounts to be paid”. This negotiating agreement was upheld by the Court of Appeal, principally because the object of the negotiations (i.e. reasonable extra costs) were tightly defined and could be determined by the court if needs be. The outcome is likely to have been very different if the parties had not agreed that reasonable extra costs were to be paid and only agreed to negotiate in good faith over a price in general terms.

Conclusions and implications

The *Brooke Homes* decision appears to be the farthest the English courts have come to date in upholding an agreement to use reasonable or best endeavours to conclude an agreement. The decision goes much further than *Petromec* because the agreement to be reached was not over some discrete matter such as a costing, but on a complete agreement for the sale of land. Nevertheless, it is clear from the judgment that it was crucial that the key aspects of the sale had already been agreed by the parties in the Agreements. What was lacking was a formal sale agreement, which precisely identified the land to be sold and dealt with other mechanics of sale. These more minor details were able to be left to the parties’ reasonable endeavours without, it seems, engaging English law’s general antipathy toward “agreements to agree”.

Parties should, however, still exercise caution when including such obligations in their agreements. Enforceability was conceded in this case and so was not fully explored in the judgment. Endeavours clauses are also inherently uncertain and their precise requirements will always depend on the context in which they are deployed. Where possible, the actions the parties are expected to take to try and fulfil the desired outcome should be set out in the agreement itself. Where an endeavours obligation is accepted, it is prudent to keep an “endeavours register” recording the steps/actions taken (and reasons for not taking a step/action) towards the object or result to which the endeavours obligation is directed.

References:

Phillips Petroleum Co UK v Enron Europe Ltd [1997] CLC 329; *Petromec Inc v Petroleo Brasileiro SA Petrobras* (No 3) [2005] EWCA Civ 891; *Multiplex Constructions UK Ltd v Cleveland Bridge UK Ltd* [2006] EWHC 1341 (TCC); *Brooke Homes (Bicester) Limited v Portfolio Property Partners Limited* [2021] EWHC 3015 (Ch).



Deemed design liability

Two recent cases from Scotland have considered the interpretation of deemed design liability clauses in consultant appointments. In one case the consultant in question was found to be liable for designs which had pre-dated its appointment and which had been proposed without its involvement. In an earlier case, a similar clause had been given a narrower interpretation in a multi-disciplinary design setting. Such deeming clauses are often used on international construction projects to provide a single point for design responsibility or to avoid gaps in liability.



Arbitration Appeal No 1 of 2021

The arbitration which led to this appeal arose from a project for the rehabilitation of a water mains system. A design and build contract was entered into for the works with a main contractor (the Contractor). The Contractor's design works were sub-contracted to a designer (the Designer) under an amended NEC Professional Services Contract 2005, Option A (the Design Contract).

Part of the works involved the use of a polyurethane lining to coat the inside of ageing pipes in the water mains. The lining material failed and the Contractor claimed against the Designer on the basis that the material chosen was inappropriate and in breach of its design obligations.

The Designer objected on the basis that the lining had been selected by the Contractor in mid-2010, long before the Design Contract was entered into in 2011. Although the Designer had been involved with the project on a letter of intent basis since early 2010, the Designer said that the selection of the lining was done without recourse to the Designer and the Designer was never asked, formally or informally, to comment on issues involving the lining.

The Contractor placed particular emphasis on two clauses in the Design Contract (the "Deeming Provisions"). The first deemed the Designer to have, *"provided for any other design works necessary to provide a complete design for the purposes of the construction works and in accordance with the Scope"*. The second deemed to be Designer's responsibility,

"any design responsibility noted as 'Construction and Design Partner' within the documents provided for within section 2 of the Scope [which was back-to-back with the Contractor's design obligations under the main contract]". The Contractor argued these provisions showed that the Designer had taken full and complete responsibility for the design.

The Contractor commenced an arbitration against the Designer and succeeded in its claim. The Designer appealed to the Scottish Court of Session.

The Court upheld the arbitrator's award. The Deeming Provisions were sufficiently clear to pass full design responsibility to the Designer. The Contractor had, *"in effect, stepped down its design responsibilities to the [Designer]"*.

The fact that the selection of the lining material had taken place prior to the Design Contract without involvement from the Designer was not something which could influence the interpretation of the Deeming Provisions. The Contractor's contract with the employer stated explicitly that no acceptance of any design work by the employer's representatives (which in any event was found to be very limited) would relieve the Contractor of its responsibilities.

The Court also rejected the Designer's submission that such a broad interpretation of the Deeming Provisions would result in absurdity. In the Court's view: *"It is not an absurd result to have responsibilities passed to others, whether ... those others are up or down the line."*



Midlothian Council v Bracewell Stirling Architects

This earlier case, decided in 2018, involved a GBP 12m damages claim for loss at a Midlothian housing development, where the homes were rendered uninhabitable due to carbon dioxide leaking from disused mining works underneath. Bracewell were appointed as the lead design consultant and agreed to be *“fully responsible for the whole design”* notwithstanding *“the stage to which the design ... has been developed prior to the Consultant having been appointed”*. However, the contract also stated that Bracewell were responsible for the performance of any sub-contractors to whom it had delegated work.

Sub-contractors appointed by Midlothian Council had carried out the ground investigations, which failed to identify the CO₂. The Inner House of the Court of Session had to decide whether Bracewell, having full responsibility contractually for design, was responsible for the designs of the council-appointed sub-contractors.

The Inner House considered that the wording of the appointment was not sufficient to impose strict liability on Bracewell for the design failings of third parties with whom it was not in contract. Its responsibility for *“the whole design”* was intended to embody the architect’s usual responsibilities for overall co-ordination of the design works. It was *“not to be construed as an acceptance of liability for anything that might ultimately go wrong with the design, no matter what its cause.”* It was also of note that the clause preserving Bracewell’s liability for sub-consultants mentioned only those sub-consultants appointed by Bracewell.

The Inner House also noted a strong commercial rationale against the imposition of such broad design responsibility:

“Although it may be open to a commercial enterprise to assume responsibility for the actions of another, with whom they have had no contractual relationship, whose specialist expertise would be outwith their own skill base and whose appointment preceded their own, it would be an unusual step and one carrying very considerable risks.”

Conclusions and implications

These two decisions provide an informative contrast as to the use of deemed design liability provisions in consultant appointments. They show that the interpretation of such provisions can vary significantly depending on the context in which they are used. In *Arbitration Appeal No. 1*, it was unexceptional that the Contractor wished to step-down its entire design responsibility to the Designer, even where that involved responsibility for design decisions which the Designer had not been involved in. The different circumstances prevailing in *Midlothian*, and particularly the involvement of other third-party consultants, made a similar proposition of reposing entire design responsibility in a single designer a highly unusual one. Parties should therefore give careful consideration to the operation of such clauses in consultant appointments and introduce clarification where necessary.

References:

Arbitration Appeal No.1 of 2021 [2021] CSOH 41; *Midlothian Council v Bracewell Stirling Architects* [2018] CSIH 21.





Cross-border enforcement of statutory adjudication decisions

Statutory adjudication for construction disputes is quickly becoming the norm in common-law jurisdictions. The UK, Australia, Singapore, Ireland and Canada all have statutory adjudication regimes and adjudication is regularly provided for by contract elsewhere. A relatively unexplored question is the extent to which the local courts of such jurisdictions will enforce an adjudication decision obtained pursuant to the statutory regime where the construction contract specifies a foreign law and jurisdiction is to govern the contract. This issue has recently been considered by the English Technology and Construction Court (“TCC”) as we discuss further below.



Cross-border adjudication disputes: the jurisdictional framework

In the UK, The Housing Grants, Construction and Regeneration Act 1996 (as amended) (the Construction Act) provides for a mandatory adjudication scheme in construction contracts. The Act applies to contracts which relate to the carrying out of construction operations in the UK regardless of whether a foreign system of law is otherwise applicable to the contract.

Whilst the right to adjudicate is unaffected by clauses which confer exclusive jurisdiction on the courts of a foreign State, it has previously been unclear whether such clauses would require the enforcement of an adjudication decision in the foreign jurisdiction or whether the UK courts, such as the TCC, would retain a residual jurisdiction in relation to enforcement.

Prior to the UK's departure from the European Union, such questions in relation to other EU countries fell to be resolved by the Brussels Recast Regulation. These regulations no longer apply from 1 January 2021 and have been replaced by legislation giving effect to the Hague Convention on Choice of Court Agreements 2005 (the Hague Convention). The Hague Convention rules apply to cross-border disputes involving EU countries and certain other jurisdictions including Singapore.

Under the Hague Convention, where parties have agreed to confer exclusive jurisdiction on a country which has acceded to the Convention, that choice must be honoured. If proceedings are commenced in a different country, the Convention requires the courts of that country to dismiss the proceedings subject to certain exceptions. One of those exceptions, contained in Article 7, concerns "interim measures" and states that:

"interim measures of protection are not governed by the Convention. This Convention neither requires nor precludes the grant, refusal or termination of interim measures of protection by a court of a Contracting State and does not affect whether or not a party may request or a court should grant, refuse or terminate such measures".

A similar exception is found in the Brussels Recast Regulation and the Lugano Convention. A recent TCC decision has considered whether this exception applies to adjudication enforcement proceedings.

Motacus Constructions Limited v Paolo Castelli SPA

This dispute concerned a supply and installation agreement for fit-out works to a hotel in London. An adjudication decision was obtained by Motacus for the payment of GBP 454,678,65 from Paola Castelli. Payment was not made in accordance with the adjudicator's decision.

Motacus applied to the TCC for summary judgment to enforce the decision. However, the contract was subject to Italian law and gave exclusive jurisdiction to the French courts. Paola Castelli defended enforcement on the basis that the English courts did not have jurisdiction to enforce the decision.

Applying Article 7 of the Hague Convention, the TCC decided that the enforcement of adjudication decisions was an interim measure of protection:

"In my judgment, the concept of an interim protective measure extends to a decision of an adjudicator which, by the operation of the 1996 Act and the Scheme, is not final and binding on the parties. The function of the adjudicator's decision is to protect the position of the successful party on an interim basis pending the final resolution of the parties' dispute through the normal court processes (or by arbitration)."

The Convention is clear that a court that grants an interim measure does so under its own law. Therefore, the TCC could accept jurisdiction and enforce the adjudicator's decision by granting summary judgment.

Conclusions and implications

This decision reinforces a key purpose of the UK statutory adjudication regime to allow the quick resolution of construction disputes on an interim basis with a view to improving cash flow. The TCC has applied this "pay now, argue later" principle to bring adjudication within the "interim measures" exception to the enforceability of an exclusive jurisdiction clause. While this decision considers only the Hague Convention, the prevalence of "interim measures" exceptions in other contexts makes it of potentially wider application.

Although not raised by Paola Castelli in this case, a potential challenge to the Court's reasoning might be made by reference to the UK Supreme Court's decision in the *Bresco v Lonsdale* decided in 2020. In that case,

the Supreme Court overturned the Court of Appeal's finding that an adjudication by a company in liquidation which could never be enforced would be an exercise in futility and could be stopped by an injunction. The Supreme Court drew attention to the wider purpose of adjudication as a dispute resolution tool in its own right:

"A very important underlying objective, both of adjudication and of other recommendations which were eventually implemented in the 1996 Act, was the improvement of cash flow to fund ongoing works on construction projects. ... But solving the cash flow problem should not be regarded as the sole objective of adjudication. It was designed to be, and more importantly has proved to be, a mainstream dispute resolution mechanism in its own right, producing de facto final resolution of most of the disputes which are referred to an adjudicator. ... There is a chorus of observations, from experienced TCC judges and textbook writers to the effect that adjudication does, in most cases, achieve a resolution of the underlying dispute which becomes final because it is not thereafter challenged."

These comments do not sit easily with the findings in *Motacus* that "the function" of an adjudication is to protect the position of the successful party "on an interim basis". If adjudication is truly to be conceived as a "mainstream dispute resolution mechanism in its own right" which in most cases results in a "de facto final resolution" it may be less capable of characterisation as an "interim protective measure".

References:

Bresco Electrical Services Ltd v Michael J Lonsdale (Electrical) Ltd [2020] UKSC 25; *Motacus Constructions Ltd v Paolo Castelli SpA* [2021] EWHC 356 (TCC).





International English Law Construction Contacts

**Paul Smith**

Partner, Energy Projects & Construction
Practice Group Manager (London)
T +44 20 7367 3475
E paul.smith@cms-cmno.com

**David Parton**

Partner, Head of Construction (London)
T +44 20 7524 6873
E david.parton@cms-cmno.com

**Steven Williams**

Partner, Co-Head of ICE Disputes (London)
T +44 20 7524 6713
E steven.williams@cms-cmno.com

**Adrian Bell**

Partner, Co-Head of ICE Disputes (London/Dubai)
T +44 20 7367 3558
E adrian.bell@cms-cmno.com

**Matthew Taylor**

Partner, ICE Disputes (London)
T +44 20 7524 6341
E matthew.taylor@cms-cmno.com

**Phillip Ashley**

Partner, ICE Disputes (London)
T +44 20 7367 3728
E phillip.ashley@cms-cmno.com

**Robert Wilson**

Partner, ICE Disputes (London)
T +44 20 7367 3682
E rob.wilson@cms-cmno.com

**Sarah Grenfell**

Partner, ICE Disputes (London)
T +44 20 7367 3549
E sarah.grenfell@cms-cmno.com

**Terry de Souza**

Consultant, Construction (London/Dubai)
T +44 20 7367 3504
E terry.desouza@cms-cmno.com

**Aidan Steensma**

Of Counsel, ICE Disputes (London)
T +44 20 7367 2137
E aidan.steensma@cms-cmno.com

**Emma Schaafsma (Kratochvilova)**

Partner, ICE Disputes (London)
T +44 20 7367 2316
E emma.schaafsmakratochvilova@cms-cmno.com

**David Moore**

Partner, Projects/Construction (Dubai)
T +971 4 374 2829
E david.moore@cms-cmno.com

**Greg Sibbald**

Partner, ICE Disputes (Dubai)
T +971 4 374 2858
E greg.sibbald@cms-cmno.com

**Kelvin Aw**

Partner, ICE Disputes (Singapore)
T +65 6422 2841
E kelvin.aw@cms-holbornasia.com

**Lynette Chew**

Partner, ICE Disputes (Singapore)
T +65 6422 2840
E lynette.chew@cms-holbornasia.com

**Jeremie Witt**

Partner, ICE Disputes (London & Brisbane)
T +61 7 3184 9111
E jeremie.witt@cms-cmno.com

CMS offices

The Americas

Bogotá
Lima
Mexico City
Rio de Janeiro
Santiago de Chile

Europe

Aberdeen	Edinburgh	Lyon	Sheffield
Amsterdam	Frankfurt	Madrid	Skopje
Antwerp	Funchal	Manchester	Sofia
Barcelona	Geneva	Milan	Stavanger
Belgrade	Glasgow	Monaco	Strasbourg
Bergen	Hamburg	Munich	Stuttgart
Berlin	Istanbul	Oslo	Tirana
Bratislava	Kyiv	Paris	Utrecht
Bristol	Leipzig	Podgorica	Vienna
Brussels	Lisbon	Poznan	Warsaw
Bucharest	Liverpool	Prague	Zagreb
Budapest	Ljubljana	Reading	Zurich
Cologne	London	Rome	
Duesseldorf	Luxembourg	Sarajevo	

Algiers
Casablanca
Johannesburg
Luanda
Mombasa
Nairobi

Africa

Abu Dhabi
Dubai
Muscat
Tel Aviv

Middle East

Beijing
Hong Kong
Shanghai
Singapore

Asia-Pacific



Your free online legal information service.

A subscription service for legal articles
on a variety of topics delivered by email.
cms-lawnow.com

.....
CMS Cameron McKenna Nabarro Olswang LLP
Cannon Place
78 Cannon Street
London EC4N 6AF

T +44 (0)20 7367 3000
F +44 (0)20 7367 2000

The information held in this publication is for general purposes and guidance only and does not purport to constitute legal or professional advice.

CMS Cameron McKenna Nabarro Olswang LLP is a limited liability partnership registered in England and Wales with registration number OC310335. It is a body corporate which uses the word "partner" to refer to a member, or an employee or consultant with equivalent standing and qualifications. It is authorised and regulated by the Solicitors Regulation Authority of England and Wales with SRA number 423370 and by the Law Society of Scotland with registered number 47313. It is able to provide international legal services to clients utilising, where appropriate, the services of its associated international offices. The associated international offices of CMS Cameron McKenna Nabarro Olswang LLP are separate and distinct from it. A list of members and their professional qualifications is open to inspection at the registered office, Cannon Place, 78 Cannon Street, London EC4N 6AF. Members are either solicitors or registered foreign lawyers. VAT registration number: 974 899 925. Further information about the firm can be found at cms.law

© CMS Cameron McKenna Nabarro Olswang LLP

CMS Cameron McKenna Nabarro Olswang LLP is a member of CMS Legal Services EEIG (CMS EEIG), a European Economic Interest Grouping that coordinates an organisation of independent law firms. CMS EEIG provides no client services. Such services are solely provided by CMS EEIG's member firms in their respective jurisdictions. CMS EEIG and each of its member firms are separate and legally distinct entities, and no such entity has any authority to bind any other. CMS EEIG and each member firm are liable only for their own acts or omissions and not those of each other. The brand name "CMS" and the term "firm" are used to refer to some or all of the member firms or their offices. Further information can be found at cms.law