The conclusion and interpretation of contracts: "pro-contractual" trends

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19 October 2017

Atkin Chambers Barristers

Agenda

1. Contract formation
2. Contractual interpretation
3. "Contra proferentem rule" & the **Canada Steamship** rule
4. Excluding (or limiting) liability for "indirect" and "consequential" loss

Contract formation

The basic requirements of a contract are that:

1. the parties have reached an agreement [not necessarily offer and acceptance], which
2. is intended to be legally binding,
3. is supported by consideration [i.e. will not enforce a promise for which nothing at all is done in return – unless in a deed], and
4. is sufficiently certain and complete to be enforceable

(see e.g. Burrows, "A Restatement of the English Law of Contract" (2016) section 2).

All 4 in issue in **Blue v Ashley** [2017] EWHC 1928 (Comm), 26/7/17…

Horse and Groom

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1. Contract formation.

- Michael Ashley owned the majority of Sports Direct's shares. Jeffrey Blue was a consultant.
- Jan 2013: Blue & Ashley met in the H&G with 3 reps of a potential broker for SD. Alcohol consumed…
- Conflicting evidence on what was said. E.g. [at #13]: Blue's evidence was that Ashley said words to the following effect:

"*What should I do to incentivise Jeff* [Blue]*? If he can get the stock to £8 per share why should I give a fuck how much I have to pay him, as I will have made so much money it doesn't matter. So let's say if Jeff can get the stock to £8 per share in the next three years, I'll pay him £10 million. Jeff: what do you think?*" [the "Offer"?!]

1. Contract formation.

- Ashley gave evidence that he recalled talking about SD's share price and how much he would be worth at different hypothetical share prices but did not recall any discussion of paying Mr Blue a sum of money if the SD share price reached £8 per share. Mr Ashley accepted that such a conversation may have taken place but said that, if it did, it would have been in the context of general banter about the share price and it would have been obvious that he was joking [#15].
- Other 3 reps gave varying evidence of what was said.
- Share price at the time was £4. In 2014, the share price hit £8 and Ashley paid Blue £1m (perhaps Blue's best point).

1. Contract formation.

- Leggatt J: "*It is rare in modern commercial litigation to encounter a claim, particularly a claim for millions of pounds, based on an agreement which is not only said to have been made purely by word of mouth but of which there is no contemporaneous documentary record of any kind. In the twenty-first century the prevalence of emails, text messages and other forms of electronic communication is such that most agreements or discussions which are of legal significance, even if not embodied in writing, leave some form of electronic footprint. In the present case, however, such a footprint is entirely absent.*" [#65]
  - See though **Berezovsky v Abramovich** [2012] EWHC 2463 (Comm)
  - USD 5.6 billion!
  - Oral agreements alleged, including at the Dorchester Hotel
  - Claims dismissed.
- Evidence based on memory [#65-70], incl.: "*the best approach for a judge to adopt in the trial of a commercial case is to place little if any reliance on witnesses' recollections of what was said in meetings and conversations, and to base factual findings on inferences drawn from the documentary evidence and known or probable facts*" [#67]

1. Contract formation.

Held (dismissing Blue's claim):

1. oral "agreement" between Ashley and Blue that, if Blue could get SD share price to £8 per share, Ashley would pay Blue £15m [#79].
2. when Ashley said he would pay Blue £15m if he could get SD's share price to £8 per share, this would not reasonably have been understood as a serious offer capable of creating a legally binding contract [#80].
3. consideration "rightly" [#60] not disputed at trial. "*The decision of the Court of Appeal in* ***Williams v Roffey Bros & Nicholls (Contractors) Ltd*** *[1999] 1 QB 1 effectively rendered the rule obsolete by accepting that performance or a promise to perform an existing duty can satisfy the requirement of consideration by providing a practical benefit to the other party, which it will invariably do*" [#59] Watch this space!
4. Blue failed *"to prove that a particular period was agreed within which the share price had to reach £8. That gap is not one which the court can fill… only possible [to imply a reasonable time term] when a court can apply some yardstick of what is reasonable… As Mr Blue has failed to prove that a specific period was agreed, I conclude that the "offer" made by Mr Ashley could not create a contract for the further reason that it lacked an essential term*" [#136].

2. Interpretation. Have we "rowed back" from using the factual matrix?

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- **Wood v Capita Insurance Services Ltd** [2017] UKSC 24, 29/3/17
- Capita ("**Buyer**") bought from Wood ("**Sellers**") the entire issued share capital of a company offering motor insurance for classic cars ("**Company**").
- Shortly after the sale, it was discovered that the Company's telephone operators had misled many customers to make a sale.
- The Buyer and the Company informed the Financial Services Authority ("FSA"). They agreed to pay compensation to customers affected by the mis-selling.

2. Interpretation. Have we "rowed back" from using the factual matrix?

- Sale and Purchase Agreement ("**SPA**"), indemnity clause:

  "*the Sellers undertake to pay to the Buyer an amount equal to the amount which would be required to indemnify the Buyer […] against* **[1]** *all actions, proceedings, losses, claims, damages, costs, charges, expenses and liabilities suffered or incurred, and* **[2]** *all fines, compensation or remedial action or payments imposed on or required to be made by the Company* ***following and arising out of claims or complaints registered with the FSA*** *… against the Company, the Sellers or any Relevant Person and which relate to the period prior to the Completion Date pertaining to any misselling or suspected mis-selling of any insurance or insurance related product or service*".

  [numbers in square brackets added to show the Buyer's case]

2. Interpretation. Have we "*rowed back*" from using the factual matrix?

- High Court: the Sellers must indemnify the Buyer even if there had been no claim or complaint.
- Court of Appeal disagreed: indemnity confined to loss arising out of a claim or complaint.
- The Buyer appealed: CA had wrongly been influenced by the Sellers' submission that the decision of the Sup. Ct. in **Arnold v Britton** [2015] AC 1619 had "*rowed back*" from the guidance on contractual interpretation which the Sup. Ct. gave in **Rainy Sky SA v Kookmin Bank** [2011] 1 WLR 2900 [#8]. This had caused the CA to pay too much regard to the words of the SPA and too little to the factual matrix.

2. Interpretation. Have we "*rowed back*" from using the factual matrix?

- Sup. Ct.: unanimously dismissed the Buyer's appeal. The CA was correct.
- **Rainy Sky** and **Arnold** said the same thing [#14]. Cf **Investors Compensation Scheme Ltd v West Bromwich Building Society** [1998] 1 WLR 896, pp 912-913, Lord Hoffmann
- The Buyer's suggested interpretation was rejected for two reasons.
- (a): the suggestion that only the "*fines, compensation or remedial action or payments imposed on the Company*" had to arise out of complaints made to the FSA against the Company [**2 above**] would not restrict the scope of the warranty in any way. The source of loss and damage in the rest of the clause [**1 above**] would remain unlimited.
- (b): it would have the effect that the clause would fail to specify against whom the relevant actions, proceedings and claims in the remainder of the clause [**1 above**] could be made. There must be a limit on who such persons could be as it would be absurd for Capita to have a claim against the Sellers for indemnity resulting from any misselling on its part before the Completion Date.
- The contractual context was also significant. The mis-selling which the indemnity clause addressed was also covered by warranties, which concern compliance and regulatory matters. The scope of the indemnity clause (which gives rise to a liability unlimited in time), must be assessed in the context of the detailed and time-limited warranties [#27].

2. Interpretation. The “slender thread”.

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- **MT Højgaard A/S v E.ON Climate & Renewables UK Robin Rigg East Limited and another** [2017] UKSC 59, 3/8/17
- 2 offshore wind farms designed and installed by MT Højgaard A/S ("**MTH**") for **E.ON**. Foundations failed shortly after completion of the project. Who was responsible for remedial costs of €26.25m?
- Technical Requirements ("**TRs**") in tender docs required the foundations to be in accordance with standard **J101**.
- J101 included mathematical formulae to calculate aspects of the foundation structures. One such formula was wrong by a factor of 10 -> strength of the foundations substantially over-estimated.

2. Interpretation. The "slender thread".

- High Court: MTH liable. Clause 8.1(x) of this contract stated that MTH should carry out the works so that they shall be "fit for its purpose". "Fit for Purpose" was defined to include adherence to the TRs. TRs, para 3.2.2.2 (and para 3b.5.1).
- 2nd limb of para 3.2.2.2: "*The design of the foundations shall ensure a lifetime of twenty years in every aspect without planned replacement.*"
- Court of Appeal: MTH appeal unanimously allowed. Inconsistency between (1) the TRs, para 3.2.2.2 (and para 3b.5.1) and (2) other contractual provisions (in particular adherence to J101). (2) should prevail. TRs, para 3.2.2.2 (& para 3b.5.1): "*too slender a thread upon which to hang a finding that MTH gave a warranty of 20 years life for the foundations*" [Jackson LJ, #106].
- Sup. Ct.: PTA refused, then allowed. E.ON's appeal unanimously allowed.

2. Interpretation. The "slender thread".

Supreme Court's summary:

- MTH liable for infringing the TRs, para 3.2.2.2 (and para 3b.5.1) whether it is a warranty that the foundations will actually have a lifetime for 20 years or an undertaking to provide a design that can objectively be expected to have a lifetime of 20 years. The foundations neither had a lifetime of 20 years, nor was their design fit to ensure one.
- J101 and para 3.2.2.2. are part of the same contract. The reconciliation of various terms in a contract, and the determination of their combined effect must be decided by reference to ordinary principles of contractual interpretation.
- The courts are generally inclined to give full effect to the requirement that the item as produced complies with the prescribed criteria, even if the employer has specified or approved the design. Thus, generally speaking, the contractor is expected to take the risk if he agreed to work to a design which would render the item incapable of meeting the criteria to which he has agreed. The TRs expressly prescribe only a minimum standard. It was MTH's responsibility to identify areas where the works needed to be designed in a more rigorous way. Further, it was contemplated that MTH might go beyond certain standards, including J101.
- TRs, para 3.2.2.2 is not too weak a basis (or too slender a thread) on which to say that MTH had a liability to warrant that the foundations would survive for 20 years or would be designed so as to achieve 20 years of lifetime. Applying the ordinary principles of interpretation, in a complex contract, this interpretation gives way to the natural meaning of para 3.2.2.2 and is not improbable or unbusinesslike.

3. "Contra proferentem rule"

- Lewison, The Interpretation of Contracts, 6th ed., #7.08:

  "***The meaning of the maxim***

  A literal translation of the principle is "the words of documents are to be taken strongly against the one who puts forward". However, the phrase "the one who puts forward" is ambiguous. It might mean:

  (1) the person who prepared the document as a whole;

  (2) the person who prepared the particular clause;

  (3) the person for whose benefit the clause operates.

  This ambiguity has led to the principle having been formulated in many different ways over the years, and as a result the formulations are not always entirely cohesive."

The “contra proferentem rule” dates back to the Romans

"Contra proferentem rule"

- Growing reluctance to apply the contra proferentem rule.
- **K/S Victoria Street v House of Fraser (Stores Management) Ltd** [2011] EWCA Civ 904; [2012] Ch 497, Lord Neuberger MR, at #68:

  "…Quite apart from raising abstruse issues as to who is the proferens (and, in particular, whether the issue turns on the precise facts of the case or hypothetical analysis), "rules" of interpretation such as contra proferentem are rarely decisive as to the meaning of any provisions of a commercial contract. The words used, commercial sense, and the documentary and factual context, are, and should be, normally enough to determine the meaning of a contractual provision."
- See also **Transocean Drilling UK Ltd v Providence Resources PLC** [2016] EWCA Civ 372; [2016] 2 Lloyd's LR 51, Moore-Bick LJ, #20-21.

"Contra proferentem rule": exclusion clauses

- **Persimmon Homes Ltd and others v Ove Arup & Partners Ltd and another** [2017] EWCA Civ 373, 25/5/17
- A consortium of housebuilders engaged Arup to provide engineering services for the development of Barry Docks in Wales. Those services were wide-ranging and included contamination investigation.
- When groundworks started, asbestos was encountered. The consortium claimed that Arup negligently failed to advise it of the extent of the asbestos. It said that, as a result, it overpaid £2m for the site and incurred extra costs owing to the late discovery of the asbestos. Before deciding upon any negligence, the court considered an exclusion clause in the contractual terms agreed between the parties.
- The exclusion clause's key words were: "***Liability for any claim in relation to asbestos is excluded.***"

"Contra proferentem rule": exclusion clauses

- Consortium relied upon the contra proferentem rule as requiring any ambiguity in an exclusion clause to be resolved against the party who put it forward and relies upon it.
- Unfortunately for the consortium, there was no ambiguity in Arup's exclusion clause.
- The Court of Appeal emphasised that the contra proferentem rule "*now has a very limited role*" [#52].
- For a contract between businesses of similar bargaining power, the courts will not artificially interpret an exclusion clause against the party relying upon it.

Canada Steamship rule: narrow limits

- Second, the consortium relied upon the rule set out in **Canada Steamship Lines Ltd v The King** [1952] AC 192, PC. Based on judgments going back over 150 years.
- The underlying basis for the rule (now) is that negligence is more serious than non-negligent, strict, liability. As a result, liability for negligence is only excluded when it is clear that the parties specifically intended it from the words used or the circumstances.
- The Court of Appeal suggested that the rule should not apply to exclusion clauses (when A excludes his liability to B) and should be marginalised to indemnities (when B must compensate A for the consequences of A's own negligence).
- In any event, it mattered not: Arup's exclusion clause clearly covered any negligence in relation to asbestos.

Canada Steamship: narrow limits

"Contra proferentem rule": limitation clauses

- **Ailsa Craig Fishing Co Ltd v Malvern Fishing Co Ltd** [1983] 1 W.L.R. 964, HL, Lord Wilberforce:

"*Clauses of limitation are not regarded by the courts with the same hostility as clauses of exclusion; this is because they must be related to other contractual terms, in particular to the risks to which the defending party may be exposed, the remuneration which he receives and possibly also the opportunity of the other party to insure.*"

- Lewison, The Interpretation of Contracts, 6th ed., #12.16:

"The High Court of Australia has rejected a rigid distinction between clauses that exclude liability and clauses that limit liability,246 and this may well come to represent English law as well. One possible route to this conclusion was suggested by Evans L.J. in **BHP Petroleum Ltd v British Steel Plc** [2000] 2 Lloyd's Rep. 277:

"*I think it is unfortunate if the present authorities cannot be reconciled on the basis that no categorization is necessary and of a general rule that the more extreme the consequences are, in terms of excluding or modifying the liability that would otherwise arise, then the more stringent the courts' approach should be in requiring that the exclusion or limit should be clearly and unambiguously expressed.*"

In the author's opinion this is a sound approach. The approach advocated by Evans L.J. in **BHP Petroleum Ltd v British Steel Plc** may be gaining ground. In **Société Générale, London Branch v Geys** [2012] UKSC 63; [2013] 1 A.C. 523, Lord Hope said:

"*As Lord Dunedin said in **W&S Pollock & Co v Macrae** 1922 S.C. (HL) 192 at 199, in order to be effective such clauses must be 'most clearly and unambiguously expressed.' In **Ailsa Craig Fishing Co Ltd v Malvern Fishing Co Ltd** Lord Fraser of Tullybelton said that it was an ordinary principle that such conditions must be construed strictly against the proferens. The principle is commonly applied in cases where the contract which the other party has entered into with the proferens is in a standard form or in terms set out by the proferens which were not negotiable. The more improbable it is that the other party would agree to excluding the liability of the proferens, the more exacting the application of the principle will be.*""

"Contra proferentem rule": time bar clauses

- Lewison, The Interpretation of Contracts, 6th ed., #12.17: "*Since a time bar clause does not wholly remove the right of an injured party to claim against the other, it is submitted that it is more analogous to a limitation clause than to an exemption clause. In other words it limits a claim temporally rather than quantitatively. Nevertheless, it is clear that the time limit within which a claim must be made must be complied with strictly.*"
- **Waterfront Shipping Company Ltd v Trafigura AG** [2007] EWHC 2482 (Comm), Gloster J (now Gloster LJ), #15:

  "*words in a time-bar provision must be given their ordinary and natural meaning. A time-bar provision is, or is closely analogous to, a limitation clause. Thus, the especially exacting principles of construction that apply to exemption clauses probably do not apply to time-bar provisions; see Lewison, The Interpretation of Contracts, 2nd edition para 11.15* ***[now above]****. The contra proferentem rule is only invoked as a last resort if the meaning of the words is so finely balanced that the contra preferentem rule should be applied in favour of Owners; see* ***Mira Oil Resources of Tortola v Bocimar, "The Obo Venture"*** *[1999] 2 Lloyd's Rep 101, [1999] 1 All ER (Comm) 732 per Colman J at 104*"
- **Multiplex Constructions (UK) Ltd v Honeywell Control Systems Ltd (No. 2)** [2007] EWHC 447 (TCC), Jackson J (later Jackson LJ), #103:

  "*Contractual terms requiring a contractor to give prompt notice of delay serve a valuable purpose; such notice enables matters to be investigated while they are still current. Furthermore, such notice sometimes gives the employer the opportunity to withdraw instructions when the fi nancial consequences become apparent.*"

Interpretation of EOT clauses

- **North Midland Building Ltd v Cyden Homes Ltd** [2017] EWHC 2414 (TCC), 2/10/17, Fraser J, #3-5:
- EOT clause 2.25 (in amended JCT Design and Build Contract 2005 form), dealing with delay where:

  "1. any of the events which are stated to be a cause of delay is a Relevant Event; and

  2. completion of the Works or of any Section has been or is likely to be delayed thereby beyond the relevant Completion Date,

  3. and provided that

  (a) the Contractor has made reasonable and proper efforts to mitigate such delay; and

  (b) any delay caused by a Relevant Event which is concurrent with another delay for which the Contractor is responsible shall not be taken into account

  then, save where these Conditions expressly provide otherwise, the Employer shall give an extension of time by fixing such later date as the Completion Date for the Works or Section as he then estimates to be fair and reasonable."
- #9 & 18: "crystal clear" that: if there are two delaying events, Event X and Event Y, occurring at the same time and causing concurrent delay to completion of the works, with Event X otherwise entitling the claimant to an extension of time, and Event Y being "another delay for which the Contractor is responsible", then the Contractor would not be entitled to an extension of time in respect of those two delaying events.
- Declarations sought (and refused):
  - that the effect of Clause 2.25.1.3(b) is to make time at large where the claimant has a claim to an extension of time for a delay caused by a Relevant Event where that delay is concurrent with another delay for which the claimant is responsible; and
  - in such circumstances, the claimant must complete within a reasonable time and liquidated damages are void.

"Contra proferentem rule": EOT clauses

- **Multiplex Constructions (UK) Ltd v Honeywell Control Systems Ltd** [2007] EWHC 447 (TCC), Jackson J, #48-49:

  "[48] In the field of construction law, one consequence of the prevention principle is that the employer cannot hold the contractor to a specified completion date, if the employer has by act or omission prevented the contractor from completing by that date. Instead, time becomes at large and the obligation to complete by the specified date is replaced by an implied obligation to complete within a reasonable time. The same principle applies as between main contractor and sub-contractor.

  [49] It is in order to avoid the operation of the prevention principle that many construction contracts and sub-contracts include provisions for extension of time. Thus, it can be seen that extension-of-time clauses exist for the protection of both parties to a construction contract or sub-contract." (underlining added)

"Contra proferentem rule": EOT clauses

- **Multiplex**, Jackson J, #56-58:

  "[56] … *(i) Actions by the employer which are perfectly legitimate under a construction contract may still be characterised as prevention, if those actions cause delay beyond the contractual completion date.*

  (ii) Acts of prevention by an employer do not set time at large, if the contract provides for extension of time in respect of those events.

  (iii) In so far as the extension-of-time clause is ambiguous, it should be construed in favour of the contractor.

  [57] The third proposition must be treated with care. It seems to me that, in so far as an extension-of-time clause is ambiguous, the court should lean in favour of a construction which permits the contractor to recover appropriate extensions of time in respect of events causing delay. This approach also accords with the principle of construction set out by Lewison in The Interpretation of Contracts (3rd edn, 2004). That principle reads as follows:

  'Where two constructions of an instrument are equally plausible, upon one of which the instrument is valid and upon the other of which it is invalid, the court should lean towards that construction which validates the instrument.'

  [58] That principle is supported by a line of authority as set out in para 7.14 and is encapsulated in the Latin maxim, verba ita sunt intelligenda, ut res magis valeat quam pereat [Words are to be so understood that the subject-matter may be preserved rather than destroyed]." (underlining added)

4. Excluding (or limiting) liability for "indirect" and "consequential" loss

- **Transocean Drilling UK Ltd v Providence Resources PLC** [2016] EWCA Civ 372; [2016] 2 Lloyd's LR 51
- Clauses excluding or limiting liability for "indirect" or "consequential" losses.
- Traditionally interpreted as referring to second limb of **Hadley v Baxendale** (even when the parties are not from this jurisdiction)
- Move towards giving the words their natural meaning.

Conclusions

- Contract formation rules well settled. Further narrowing re consideration?
- Contract interpretation.
  - Even stricter application of words used with limited exceptions.
  - "Contra proferentem rule": "*now has a very limited role*" (**Persimmon**)
  - Other rules being narrowed, e.g. Canada Steamship rule (**Persimmon**)
  - Literal interpretation of clauses excluding (or limiting) liability for "indirect" or "consequential" loss?
- Greater contrast between interpretation of contracts in (1) the courts; and (2) arbitration and adjudication?