K&L GATES

In Site

Updating you on legal developments affecting the construction industry

Summer 2009

In this issue:

A Useful Contribution?

Arguing over net contribution clauses is a common feature of negotiating consultants' appointments and warranties. These clauses provide that, where two or more parties are jointly liable for the same loss or damage, the liability of each party is limited to the amount that a court, on a fair and reasonable basis, would apportion to that party. Consultants and their insurers want them in, whilst employers and funders strive to keep them out.

However, until the Scottish case of *Langstane Housing Association Limited v Riverside Construction (Aberdeen) Limited and Others* [2009] CSOH 52 earlier this year, there had been no court decision specifically considering the effectiveness of net contribution clauses – and in particular, whether they fall foul of the Unfair Contract Terms Act 1977 ("UCTA").

Incorporation of terms

An issue which arose in proceedings brought by the employer, Langstane, against the consulting engineer, Ramsay and Chalmers ("Ramsay"), and others for breach of contract and negligence was whether a net contribution clause was included in the terms of Ramsay's appointment.

Ramsay had initially been appointed by Langstane to a panel of consultants in 1995 on the basis of the "*current*" ACE Conditions. It was subsequently engaged on the project in question in March 2001 by a letter stating "*Basis of Engagement—ACE Conditions of Engagement Agreement B1*". The Court said it was clear that the parties intended to enter into a contract on the basis of the version of the ACE B1 conditions current at the time Ramsay was engaged on the particular project—in this case the 1998 version—rather than at the date of the panel appointment. It would be very unusual for commercial construction parties to intend all their contracts to be fixed to a point in time and thereby for older, out-of-date standard forms to apply.

Unlike earlier versions of the ACE Conditions, the 1998 version contained a net contribution clause. The Court held that the whole of ACE B1 was incorporated and there was no reason to exclude the net contribution clause. It was not a particularly onerous or unusual clause such that particular attention should have been drawn to it for it to be effectively incorporated. Relevant factors here included the fact both were commercial parties who had had a course of prior dealing on ACE terms over a number of years. The net contribution clause had been included in the ACE terms for several years by that stage, so should not have taken anyone by surprise, and significantly, it was Langstane itself who had suggested the use of the ACE terms.

On this issue, this case provides a useful reminder of the importance of being precise when agreeing terms. Considerable time and expense would have been spared here if the parties had stated clearly in 2001 that the "1998 version" of the ACE Conditions applied.

UCTA issues

After deciding that the net contribution clause was incorporated, the Court also had to consider Langstane's arguments that the clause fell foul of UCTA sections 16 and 17 and so therefore did not apply.

Section 16(1) states that, to exclude or restrict liability for breach of duty arising in the course of any business, it must be fair and reasonable to incorporate that term into the agreement. Lord Glennie decided that there was considerable force in Ramsay's argument that a net contribution clause

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did not exclude or restrict liability for its breach of duty – instead it ensured that it was only liable for the full consequence of its own breach of duty and would not be held liable, under the doctrine of joint and several liability, for the breach of duty of others. This interpretation of the intention and effect of net contribution clauses is likely to be criticised in any future case seeking to distinguish *Langstane*.

Section 17(1) imposes additional requirements where standard forms are used. Standard form terms which exclude or restrict liability to "*a customer*" have no effect unless they are fair and reasonable. Section 17(2) defines a customer as a party who deals on the basis of "*written standard terms of business of the other party*". Lord Glennie decided that for two reasons this provision did not apply to this case. Firstly, the ACE Conditions were not Ramsay's own terms of business but had been published by the ACE and are widely used by the engineering profession. Secondly, ACE Conditions had been proposed by Langstane itself as the basis of agreement.

To a considerable extent, the decision is confined to its facts, and has been criticised for the conclusions it did reach. Of particular interest is the fact that the Court went on to comment that, even if UCTA sections 16 and 17 had been applicable, it would have held the net contribution clause to be fair and reasonable. On this point, Lord Glennie commented "*If proper insurance is in place then it should be possible in the event of insolvency…to go against the insurer. I see nothing unfair or unreasonable in the client taking the risk that he has adequately covered himself against the possible insolvency of those whom he himself has appointed*". This view presupposes that insurance continues in the event of insolvency, which is not necessarily the case. The practical ability of an employer to protect itself in the event of insolvency by going directly against the professional indemnity insurer may not be successful, with the employer instead finding itself getting in line as an unsecured creditor.

It is also important to bear in mind that the case does not decide that net contribution clauses generally will be enforceable, or even that such clauses in later versions of the ACE Conditions (which are worded slightly differently) are necessarily also "fair and reasonable". The decision may be different if a consultant is using its own individual terms of business and/or contracting with a consumer (in which case UCTA is more likely to apply) or if the employer is less familiar with the existence of a net contribution clause within the standard terms (in which case particular attention may need to be drawn to it for it to be effectively incorporated).

As a Scottish case, the decision in *Langstane* will be persuasive, but not binding, on courts in England and Wales and it will be interesting to see if, and to what extent, English courts follow the decision. ■

Construction Bill Update

The Local Democracy, Economic Development and Construction Bill 2008 ("the Bill") has completed its passage through the House of Lords and is presently passing through the House of Commons. If Part 8 of the Bill becomes law, it will amend the payment and adjudication provisions of the Housing Grants, Construction and Regeneration Act 1996 ("the Act").

Changes include removing the requirement for construction contracts to be in writing (section 107 of the Act) and prohibiting "pay-when-certified" clauses. The proposed amendments to the adjudication provisions are fairly minimal, but include outlawing agreements as to costs unless made after the dispute has been referred.

Although it is anticipated that the Bill will be enacted before the end of the year, the Government has indicated that there may be a further 18 month consultation period before the Bill comes into force. We will provide a detailed examination of the final agreed amendments once parliamentary debate has concluded and the Bill has received royal assent. ■

He Who Hesitates!

Waiver provisions are often included in contracts with the intention of preserving the innocent party's rights if it decides that immediate enforcement of the other party's breach is inappropriate.

The efficacy of such provisions has however been called into question in the case of *Tele2 International Card Company SA and others v Post Office Limited* [2009] EWCA Civ 9. This case held that that where a party continues to perform under a contract when the other party is in breach, it is likely to be held to have affirmed the contract by election – irrespective of whether the contract includes a waiver clause.

The contract in this case contained a waiver clause stating that: *"In no event shall any delay, neglect or forbearance on the part of any party in enforcing… any provision of this agreement be or be deemed to be a waiver thereof…."*.

Tele2 was in material breach of contract by failing to provide parent company guarantees to Post Office Limited ("POL"). As a result POL was entitled to terminate the contract. Rather than doing so, however, it allowed performance of the contract to continue until about a year later when POL decided to terminate the contract for failure to provide the guarantees. During that time it had not protested about the absence of the guarantees.

The Court of Appeal had to decide whether, in the circumstances, the termination was valid.

Without the waiver provision, POL by its actions in continuing to perform the contract without objection would have been taken to have elected to affirm the contract. POL's rights would then have been restricted to a claim in damages and it would not be able to terminate.

Reviewing case law, the Court of Appeal decided that the waiver provision could not prevent an election from taking place. It was a matter of fact whether or not the election to abandon the right to terminate had occurred. The waiver provision did not address the issue of election or whether or not to exercise a contractual right. It did not attempt to say that the doctrine of election should not apply—*"even assuming that any contractual provision could exclude the operation of the doctrine"*.

The conclusion of the Court might come as a surprise to some in light of the provision, but when viewed in the context of a need for certainty in commercial dealings, it clearly makes sense that if a contract is to

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Waiver and Termination of Settlement Agreements

If a settlement agreement includes a waiver of existing claims, the parties should expressly state whether the waiver survives termination of the settlement agreement or not.

This issue arose in the recent Scottish case of *Robertson Construction Central Ltd v Glasgow Metro LLP* [2009] CSOH 71. The settlement agreement in this case provided that the contractor (Robertson) would complete outstanding building works in exchange for the employer (Glasgow Metro) paying an agreed sum and waiving its claim to liquidated damages under the building contract in respect of the specific matter in dispute (but not otherwise).

When the employer subsequently alleged that the contractor had failed to complete the outstanding works timeously, it terminated the settlement agreement and sought to revive its claim under the building contract. The Court held that the employer could not do this as the waiver of its claim under the building contract had survived termination of the settlement agreement. There was nothing in the settlement agreement that made the employer's waiver conditional on the contractor complying with its obligations under the settlement agreement. It would have been open to them to draft the agreement so that the waiver was dependent on future performance, but they chose not to. ■

New Standard Forms

JCT

The Joint Contracts Tribunal ("JCT") is in the midst of rolling out a complete new suite of contracts, to be known as "Revision 2 2009" to the 2005 suite. Publication of the new suite should be complete by the end of the summer. Revision 1 is being withdrawn from publication. Guides are being published alongside the new contracts.

The more significant of the amendments include the following:

- Interim payment applications can now be made every 2 months between practical completion and the end of the rectification period. This is a useful amendment meaning claims should be submitted as they arise, rather than being "held-over" to the final account. Equally importantly however, it prevents a "drip-feed" of claims every week or two.
- A new Schedule 8 has been added to the standard building contracts providing for collaborative working, cost savings/value improvements and sustainable development. These will be included in the contract by default unless de-selected in the Contract Particulars.
- Revisions to some of the default provisions for professional indemnity cover, which are unlikely to be popular with employers and funders. If the parties do not state the amount of cover for pollution and contamination claims, it is not required (previously the default position was cover at the full amount of professional indemnity cover). New provision has been added for asbestos claims, with the default position also being that no cover is required unless stated.

A detailed review of the Guide published (or yet to be published) for each of the JCT contracts is needed to identify, and gain a full appreciation of, the changes made. The JCT is not, we understand, publishing an 'Amendment 2' sheet (as it did when the new CDM Regulations necessitated amendments in 2007) which would make identification of all changes easier. The digital service will be updated approximately a month after the hard copies are available.

ACE

The Association for Consultancy and Engineering (ACE) also launched its new suite of professional appointments for consultants and engineers in May. These are known as the ACE Agreements, 2009 edition. The new suite of agreements comprises eight new forms of professional appointment and a new Schedule of Services, which has eight separate sections.

The agreements replace the ACE Agreements 2002, which were last revised in 2004. The agreements have been simplified with a focus on user-friendliness and offering greater versatility for both clients and consultants, who will be able to tailor-make the services to match the requirements of the project.

Changes include:

- The introduction of a default limit of liability of ten times the fee – which may not prove high enough for certain clients, projects, or types of services.
- Expansion and clarification of the Schedule of Fees to accommodate a wider range of fee-bases and payments for "extras", such as the provision of collateral warranties.

The agreements retain the limitations of liability that appeared in the 2002 agreements, including the net contribution clause. It appears the ACE has drawn support from the recent Scottish case of *Langstane Housing Association Ltd v Riverside Construction (Aberdeen) Ltd* (reported above). ■

Case Update

Adjudication – Liability For Adjudicator's Fees

The recent case of *Christopher Michael Linnett v Halliwells LLP* [2009] EWHC 319 (TCC) confirms the ability of an adjudicator to recover his fees from a responding party who challenges his jurisdiction and refuses to sign his terms of appointment.

Mr Linnett was appointed to adjudicate on a dispute between Halliwells and ISG InteriorExterior Plc ("ISG"). He found in favour of ISG and said that Halliwells should pay his fees and expenses.

Halliwells said it was not responsible for the fees because Mr Linnett did not have jurisdiction to adjudicate on the dispute and there was no contract between them. Halliwells challenged jurisdiction on the basis that (amongst other things) the referral notice had been served out of time. It maintained that challenge throughout the adjudication (but did not withdraw) and did not sign the adjudicator's terms.

The TCC ruled that even though Halliwells had not signed the adjudicator's terms, a contract had been formed between it and the adjudicator by its conduct and it was an implied term of this contract that Halliwells were jointly and severally responsible for the adjudicator's reasonable fees and expenses. This was the case whether or not the adjudicator had jurisdiction (which, in fact, the court found he had).

By continuing to participate in an adjudication, a party raising a jurisdictional challenge might benefit from the adjudicator's decision (either on jurisdiction or merits). The TCC noted that it is not uncommon for a party to raise a jurisdictional argument but continue to fight the claim on its merits. Although Halliwells made an assertion of lack of jurisdiction, by continuing to participate in the proceedings (even without prejudice to that contention) Halliwells were still requesting the adjudicator carry out work and make a decision.

This case demonstrates that a responding party to an adjudication, which challenges the adjudicator's jurisdiction, may still be liable for the adjudicator's fees, whether or not the adjudicator does, in fact, have jurisdiction to adjudicate. The only practical – but not necessarily realistic - way to avoid this would be to raise your jurisdictional challenge and withdraw from the adjudication. If this approach is taken, then you have not asked the adjudicator to do anything. Conversely, if you participate, you ask the adjudicator to carry out work and make a decision, even if that is simply to make a non-binding decision on jurisdiction.

Practical Completion— Challenging A Certificate

In *Menolly Investments 3 SARL v Cerep SARL & Others [2009] EWHC 516 (Ch)* a certificate of practical completion was successfully challenged on the basis that the certifier had exceeded his authority in issuing it. The case is also a caution for employers or buyers who may decide not to make a fuss about incomplete work at the time, but later find this prevents them challenging the issue of a certificate of practical completion.

Practical completion of certain construction and refurbishment works (to be completed in 2 sections) was made a condition precedent to completion of a share purchase agreement ("SPA") entered into between Menolly (as buyer) and Cerep (as seller).

The seller procured those works under a JCT Standard Form contract and appointed an employer's agent with responsibility for issuing the sectional certificates of practical completion.

The buyer sought a declaration that the section 1 certificate was invalid because (amongst other things) the building contractor had failed to provide level access, even though this was an express requirement of the contract and required by disability laws. In response, the seller argued that the

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buyer was estopped from arguing that the certificate was invalid.

The Court found that the employer's agent had acted outside his authority in certifying practical completion but the buyer was estopped from relying on that argument because of its conduct. Accordingly, all conditions precedent for completion of the SPA had been met.

The Court found that the building contract required level access. In certifying practical completion, the employer's agent had proceeded on the assumption that it was not a requirement. In doing so he had taken it upon himself to construe the contract, but there was nothing in the building contract or SPA giving him authority to do so. In deciding this, the Court recognised that it is a question of fact and degree whether or not a certifier acts within the scope of his authority and, by way of example, drew a distinction between certifying practical completion where a whole storey of a building, or a small porch, is missing. In the first example, the employer's agent would be making a manifest error and "*would not, on any objective assessment, be giving a certificate of practical completion of the works in relation to which it was his function to give or refuse a certificate*". In contrast, "*… if an insignificant part of the contracted works is missing, the works as a whole may still be practically complete*" even if, as in that example, it was an express term of the contract to provide the porch.

The Court also found however that the buyer was estopped from arguing that the certificate was invalid because of its conduct. This included acknowledging, through conduct and correspondence, that the absence of level access would not prevent practical completion (but could be dealt with via a price adjustment) and proceeding on the basis that completion of section 2 would satisfy the last remaining condition precedent under the SPA – this implied that section 1 had reached practical completion. ■

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He Who Hesitates!

be brought to an end, the party in default should know sooner rather than later where it is continuing to expend time, money and resources in otherwise performing its obligations under the contract. There should be a limit to the ability of the innocent party to hold a sword of Damocles over the head of the other party and terminate the contract at some later time when it may wish, for completely unconnected reasons, to extricate itself from its bargain, as was the case in *Tele2*. ■

Corporate Manslaughter

The first trial of a company under the Corporate Manslaughter and Corporate Homicide Act 2007 is about to start. A geotechnical firm has been charged following the death of an employee killed whilst taking soil samples on a building site. The company's director is charged with the common law offence of gross negligence manslaughter.

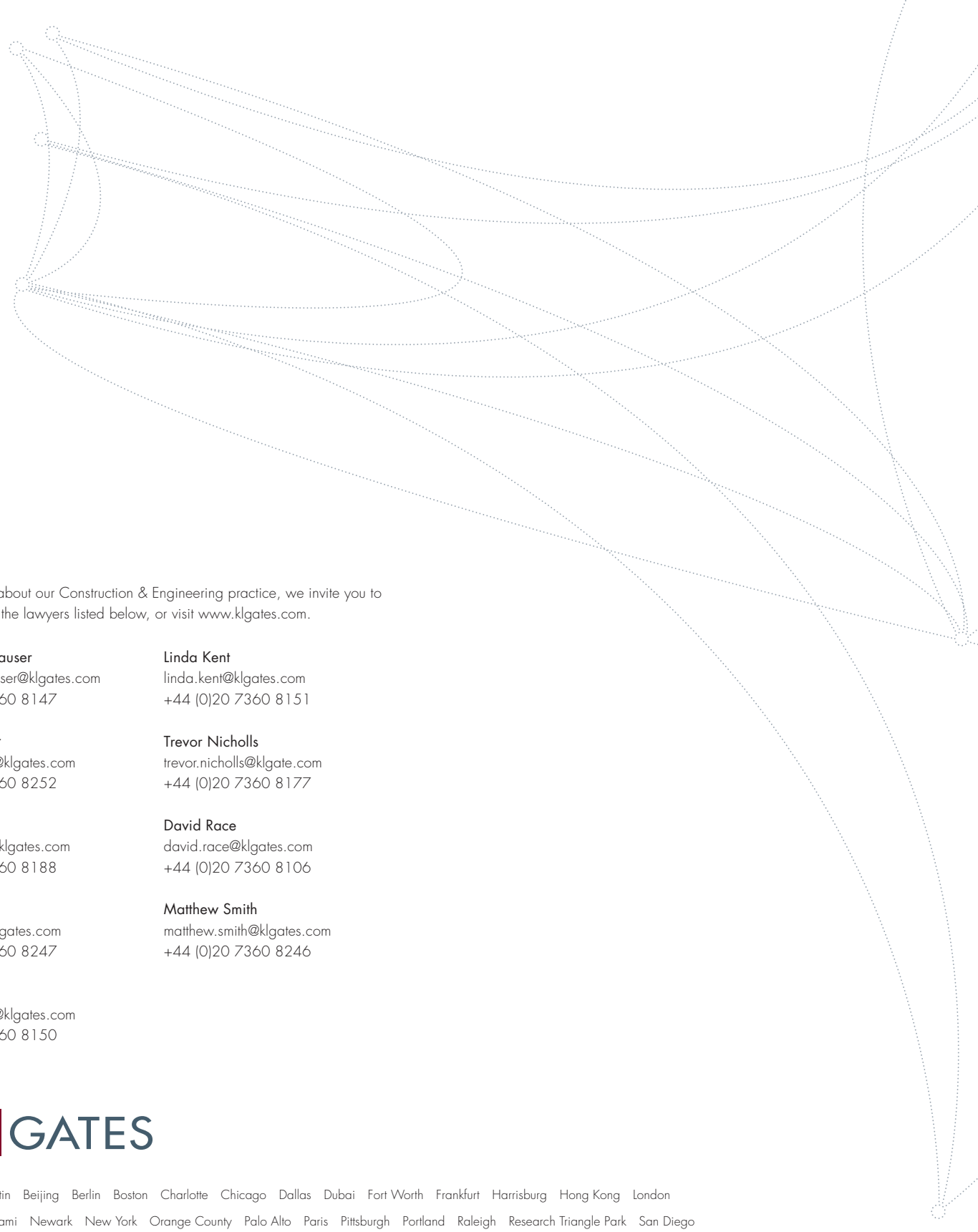
Welcome to Our New Partners

John Chandler

John joined K&L Gates from DLA Piper on 1 June 2009, where he was head of waste projects. He has closed numerous waste PFI/PPP projects in recent years, acting for local authorities and contractors. The projects he has worked on have used a variety of technologies, from mass burn incineration to mechanical biological treatment and autoclave, each with its unique set of challenges and solutions. The waste PFI/PPP market is growing rapidly as councils strive to meet their diversion from landfill and recycling targets against a background of landfill tax which is set to escalate at a rate of £8 per tonne per annum from £40 per tonne now to £72 per tonne in 2013. Over ten waste PFI/PPP projects are due to hit the market each year.

Matthew Smith

Matthew joined K&L Gates in 2000 as a senior associate and was made a partner on 1 March this year. He has a broad range of experience of contentious and non-contentious construction matters, from advising on procurement strategies for major projects to resolving contract disputes or defect claims. His main areas of practice include infrastructure and transport projects and construction insurance. He advises on the use of the NEC forms of contract and lectures regularly on the subject.



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