

## 2008/2009 Construction Law Update

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### Preamble

Perhaps it is not surprising that this year has seen a good deal of case law about adjudication and a relatively small amount of case law relating to other aspects of construction contracts.

That said there have been some useful cases on procurement. Since this is a specialist area, I am not dealing with the procurement cases today.

### Formation of Contract – Acceptance by Conduct

*A E Yates Trenchless Solutions Limited –v- Black and Veatch Limited* Construction Industry Law Letter (“CILL”) March 2009.

This is a typical “cherchez le contract” case.

The works in question were drilling works at Burrows Water Treatment Works in Devon. Gleeson engaged Yates as Sub-Contractor. The works were subsequently novated to Black and Veatch.

Gleeson’s invitation to tender stated that if it was accepted, the terms of the sub-contract would be the I Chem E Brown Book.

Yates tendered on the basis that the contract would be the ICE Blue Book.

At the tender interview the parties signed the “Record of Interview” document which recorded that the sub-contract would be the I Chem E Brown Book.

In November 2005, Gleeson emailed Yates with a sub-contract order stating that Yates should proceed with the work and the sub-contract would follow as soon as possible.

Gleeson then sent Yates sub-contract documentation including a sub-contract under the I Chem E Brown Book conditions. Yates confirmed that the sub-contract documentation had been sent to their head office for approval.

However, the contract was not signed or returned to Gleeson.

Yates made claims for additional payment to Gleeson referring to the Brown Book conditions on a number of occasions.

Yates then took legal advice which was that the Brown Book was not incorporated into the sub-contract.

The issue before the Court was whether there was a sub-contract and when it came into being.

The Court decided that the contract was made on Gleeson's terms and conditions. This was the case even though Yates had neither accepted nor rejected the sub-contract agreement expressly; Gleeson's offer had been accepted by the conduct of Yates.

The sending of the sub-contract agreement by Gleeson amounted to an offer. Sub-contract documents appear to have been mislaid by Yates.

However, Yates accepted by their conduct in:-

- a) receiving variation instructions without challenging them and acting on them;
- b) signing and returning and operating a self-billing system referred to by Gleeson;
- c) the commencement of the sub-contract works without qualification or reservation;
- d) the making of claims pursuant to the Brown Book;
- e) sending a letter indicating that it had notified claims pursuant to the Brown Book.

It is interesting that the Court referred to the earlier case of *G Percy Trentham Limited –v- Archital Luxfer Limited* 1993 1 Lloyds' Reports 25. This was a landmark case in which the Court of Appeal said that even though there was no precise correspondence between offer and acceptance, the fact that a transaction had been performed on both sides made it unrealistic to argue that there was no intention to enter into legal relations and difficult to submit that the contract was void for vagueness or uncertainty.

The Court referred to the fact that English Law generally adopts an objective approach to contract formation. It ignores the parties' personal expectations or mental reservations. The yardstick is the reasonable expectations of sensible businessmen.

In short, the Court will find the existence of a contract (and one which falls within the Housing Grants, Construction and Regeneration Act) even though it has to look to the conduct of the parties.

### **Contract Interpretation – Pre-Contractual Negotiations**

***Chartbrook Limited –v- Persimmon Homes Limited* 2009 UKHL 38, 2009 3WLR267**

This is a House of Lords case and therefore important in relation to the interpretation of contracts.

In a nutshell, the House of Lords upheld the general rule that evidence of pre-contractual negotiations is not admissible when seeking to interpret a contract. This is the case unless the wording of the contract is ambiguous.

However the rule does not exclude reliance on pre-contractual negotiations to establish that a fact which is relevant as background was known to the parties.

You can also rely upon pre-contractual negotiations if you are claiming estoppel by convention. This means that where the parties have negotiated an agreement on a common assumption, which may be an assumption that certain words

bear a certain meaning, they are prevented from saying that the word should have a different meaning. It is permissible to have regard to the pre-contract negotiations to decide whether there was or wasn't a prior common assumption.

You can also rely upon pre-contract negotiations to try to claim rectification.

The party seeking rectification must show:-

- 1) the parties had a common, continuing intention in respect of the matter to be rectified;
- 2) this was outwardly expressed;
- 3) the intention continued at the time the written agreement was made;
- 4) by mistake the agreement did not reflect that common intention.

The Chartbrook case related to the interpretation of the contract between two parties for the development of a building project on a piece of land acquired by one of them.

The principal question when trying to interpret a contract is

*"What a reasonable person, having all the background knowledge which would have been available to the parties, would have understood them... to mean"*

The Courts do not easily accept the parties have made linguistic mistakes.

The vital question was, had something gone wrong with the language used so as to justify adopting a meaning which wasn't consistent with ordinary grammar but which gave effect to the commercial purpose of the parties?

The Court decided that in this case, the ordinary meaning made no commercial sense. The Court gave effect to a proper commercial meaning.

The Court said *"In deciding whether there is a clear mistake, the Court is not confined to reading the document without regard to its background or context. The exercise is part of the single task of interpretation, the background and context must always be taken into consideration"*.

It is important to bear in mind that the Court did not depart from the normal principle that evidence should not be admitted to draw inferences as to the meaning of the contract, where the contract can be interpreted within its own four corners, except in the case of ambiguity.

When considering whether rectification should take place, based upon a prior common intention, the test is what the reasonable observer would think.

### **"The Wrong House"**

As a moment of light relief in amongst all this heavy-duty contract interpretation, please reflect on the following:-

It took the Court of Appeal (and only by a majority decision) to finally decide that a Surveyor who had valued the wrong house for mortgage purposes was liable to the funder!

Things were not quite as simple as that... they never are!

In *Platform Funding Limited –v- Bank of Scotland Plc* 2009 2 ALL ER344 the Court decided that in the normal retainer of a Surveyor to inspect and value a property there is an inherent obligation to inspect and value the right property. The valuation of a different property is a breach of contract, even though the Surveyor has not failed to act with reasonable care.

Platform Funding were asked to give a loan to Mr Hewes on a property at 1 Baker's Yard.

The Valuer was employed at the time by Colleys which is part of the Bank of Scotland. The Valuer went to site and was met by Mr Hewes. Instead of taking the Valuer to 1 Baker's Yard, which was under construction, Mr Hewes took him to 5 Baker's Yard where the property was almost complete. So the Valuer valued the wrong property.

Hewes defaulted on the mortgage and the claimants repossessed the property. The property was sold for less than the mortgage value.

Platform Funding could have claimed in negligence but they might have been able to prove that the Valuer had been negligent. The alternative was to say simply that the Bank of Scotland was liable for valuing the wrong house and it was not necessary to prove negligence. This was a restricted duty.

The Court of Appeal upheld this duty on two grounds:-

- 1) the instructions given by Platform Funding to the Valuer;
- 2) the warranty contained in the Declaration forming part of the Report

On the grounds of (1) the Valuer had failed to carry out the instructions at all. He had simply valued another property.

On the grounds of (2) – the valuation report certified that the property offered as security had been inspected by the Valuer. This amounted to a contractual warranty that 1 Baker's Yard had been inspected. This was a statement of fact and was not limited to the taking of reasonable care. Since it was unqualified it created a liability.

### **Contract Termination or Acceptance of Repudiation – the Two Alternatives**

***Stocznia Gdynia SA –v- Gearbulk Holdings Limited* – Court of Appeal – Construction Industry Law Letter, May 2009**

The case related to supplying hulls for ships.

Stocznia Gdynia was a shipbuilding yard ("the Yard). They were due to supply hulls to Gearbulk.

The contract at Article 10 set out compensation for breach of contract and excluded other forms of compensation. Article 10.7 stated that the effect of termination was that the Yard would repay Gearbulk all sums previously paid under the contract but would not be liable for liquidated damages.

The Yard did not supply 3 hulls under 3 contracts. Gearbulk terminated the contracts.

The matter went to arbitration and then to the Court at first instance and then to appeal.

The judge who heard the case first decided that Article 10 did not exclude Gearbulk's right to treat the contract as discharged by repudiatory breach or to claim damages for repudiatory breach. He did however decide that Gearbulk was precluded from claiming damages at common law for the repudiation of the 3 contracts because it had affirmed the contract through the exercising its right of termination.

The case raised the old chestnut of whether the termination provisions of the contract preclude the wronged party from treating the contract as discharged and accepting the repudiatory breach at common law. It also raised the question of whether giving notice of termination precluded Gearbulk from claiming damages at common law on the basis of the repudiation.

The Court of Appeal decided that where the circumstances for contractual termination go to the root of the contract and are repudiatory in nature, and the consequences of contractual termination and repudiation are the same then:-

- i) generally a party will be able to claim its rights to damages in repudiation in addition to any contractual remedy that it may have;
- ii) there does not have to be a clear election by the wronged party as to which method of termination is being followed.

On the other hand, if the contract and the general law provide the injured party with alternative rights that have different consequences then the wronged party will have to elect between its contractual rights and its right to accept the repudiatory breach at common law and the precise terms in which it informs the other party of its decision will be significant.

There was no good reason to treat Article 10.7 as providing an exclusive remedy so as to take away damages for repudiation.

#### **Defective Premises Act and Fitness for Habitation**

*Alexander John McMinn Bole and Stefanie van den Haak –v- Huntsbuild Limited and Richard Money* CILL May 2009

The case is relevant to those who design and build houses.

There is only a small amount of law on the Defective Premises Act. This case decided that a property can be unfit for habitation under the Act even though it has been continuously occupied. The case equates suitability for purpose in relation to house building with fitness for habitation.

Huntsbuild built a house for Mr and Mrs Bole and engaged Richard Money as Structural Engineers.

The property suffered from cracking caused by heave resulting from inadequate depths of foundations.

Section 1 (1) of the DPA says that a person taking on work in connection with the provision of a dwelling owes a duty to the person ordering the work or who subsequently acquires the dwelling to see that the work is done in a workmanlike and professional manner with proper materials so that the dwelling is fit for habitation.

Huntsbuild's defence was that it constructed the foundations in accordance with the specifications and Richard Money's drawings. Richard Money's defence was that its work was of a professional standard. The foundations were to the requisite minimum depth and Huntsbuild should have taken steps to prevent heave occurring.

General principles of law discussed include:

A house may be unfit for habitation on the basis of an imminent risk of failure, even though it is currently intact. If the support for the house from adjoining land is inadequate so that the house is on an unstable hillside, then it is unfit for its purpose.

However, the Act was designed to provide a remedy for defects which render a house unfit for habitation and not for trivial defects.

Flats have been held to be unfit for habitation due to damp.

A judge has to ask himself whether the claimant has proved on a balance of probability that the defendant's failure to do work in a workmanlike manner has caused the property to be unfit for habitation.

If the inadequacy of the foundations was inevitably going to produce a result that a house would collapse then the house is not fit for its purpose.

However, each case must be considered on its merits.

The definition in the Housing Act 1985 provides a useful checklist as to the type of defects which may be so fundamental as to render a property unfit for habitation.

The Housing Act states "*In determining for any purpose of this Act whether premises are unfit for habitation regard shall be had to their condition in respect of the following matters:*

- *repair*

- *stability*
- *freedom from damp*
- *internal arrangement*
- *natural lighting*
- *ventilation*
- *water supply*
- *drainage and sanitary conveniences*
- *facilities for the preparation of cooking the food and disposal of waste water"*

It is not appropriate to look at each room and decide in isolation whether that room is fit for habitation and if it is, to exclude that room from further consideration. A house can be unfit for habitation if a single room cannot be inhabited.

### **Adjudicator's Fees**

#### ***Mr Christopher Michael Linnett –v- Halliwell's LLP***

This case decides that where a matter is referred to adjudication and a party does not agree the Adjudicator's terms that party is nevertheless obliged to pay the Adjudicator's fees and expenses if there has been no challenge to jurisdiction.

A contract will be implied between the party and the Adjudicator by the conduct of the party in participating in the adjudication. An implied term of that contract will be to pay the Adjudicator's reasonable fees and expenses.

However, if a party makes a valid jurisdictional challenge and does not participate in the adjudication, then that party can have no liability for the fees and expenses of the Adjudicator. (Unless, presumably the challenge fails in the Courts).

On the other hand, where there is a challenge to jurisdiction and the party continues to participate in the adjudication he must still pay the Adjudicator's fees. By participating and thereby requesting the Adjudicator to adjudicate on the dispute, the party will generally be liable for the reasonable fees and expenses of the Adjudicator. Alternatively, the Adjudicator is entitled to be paid in restitution the reasonable value of the services he has provided.

### **Adjudication – the Scope of any Defence or Response – and the Right to Raise Set-Offs**

We saw last year, in the case of *Cantillon –v- Urvasco* 2008 EWHC 282 that a responding party to an adjudication is entitled to raise any matter by way of a defence that would amount in law or fact to a defence to the claim being pursued.

The Court took this a step further in the case of *Quartzelec Limited –v- Honeywell Control Systems* 2008 EWHC 3315. This case is reported in Building Law Monthly August/September 2009. The Court decided that the Adjudicator's decision was unenforceable because the Adjudicator had failed to act in accordance with natural justice in failing to consider a defence. The judge declined to sever the unenforceable part of the decision so as to allow an enforceable part to stand so that the whole decision was unenforceable.

The contract was the Ivory Form of Sub-Contract used by the Confederation of Construction Specialists. Quartzelec agreed under that contract to design, supply, install and commission communication systems for six buildings.

There was a dispute over valuation and payment.

Quartzelec served Notice of Adjudication.

Honeywell sought to reduce the value of the claim by raising an omission in the scope of the works. The Adjudicator declined to take the omission into account on the ground that the proposed reduction in price had not been in play prior to the Notice of Adjudication.

The judge said "*It is difficult to see why a Respondent should not be entitled to raise any defence open to him to defend against that claim, regardless of whether or not it was raised as a discreet ground of defence in the run up to the adjudication*".

Therefore, a claimant in an adjudication, trying to use the adjudication mechanism for the purpose for which it was intended – to secure urgent cash flow – could meet virtually any defence whether or not it had been raised before the Notice of Adjudication.

However, the case of *Letchworth Roofing Company –v- Stirling Building Company* (CILL June 2009) places some limitation on this broad principle.

Letchworth issued application no. 5 for payment of £117,286. Stirling did not pay and alleged that it had a cross claim for delay. No withholding notice was served against application 5.

Letchworth issued a Notice of Adjudication identifying the dispute as non-payment and whether a valid withholding notice was in place. Letchworth made it clear that although there was no withholding notice it was not averse to the Adjudicator deciding the merits of the cross claim and calculating the sum that might otherwise have been withheld.

The Adjudicator valued the application and ordered payment. He also valued the delay cross claim because he had been asked to do so but stated that that part of his decision was "declaratory only". Stirling refused to pay the amount ordered by the Adjudicator.

The Court affirmed the Adjudicator's decision and said that the Adjudicator should not have taken the value of the cross claim into account in ordering payment.

The Court said that a responding party cannot rely on a cross claim in adjudication which has not been the subject of a withholding notice.

In simple terms, an Adjudicator cannot take into account a cross claim that requires a withholding notice unless the withholding notice has been served.

**A Trade Association did not owe a duty of care in respect of information on its website**

*Pachett -v- Swimming Pool and Allied Trades Association 2009 All ER (D) 152*

SPATA is the trade association for swimming pool contractors. The Court of Appeal decided by a majority that SPATA did not owe a duty of care to claimants who said that they had employed a contractor in reliance on information to be found on SPATA's website.

The main reason for deciding that a duty of care was not owed was that the website encouraged readers to make further enquiry and in particular to obtain an information pack. The pack included a Contract Check List which sets out questions that the customer should ask a would-be tenderer and the appointed installer before work starts and prior to releasing the final payment.

In 2006, Mr and Mrs Pachett looked at SPATA's website and obtained from it the name of Crown Pools Limited and asked them for a quotation. Work commenced. Crown did not complete the works. The work was said to have been defective. The work was completed by another contractor. The Patchetts said they had lost £44,000.

SPATA's website stated that SPATA pool installer members were fully vetted and required to comply with a code of standards and ethics. It also said that only SPATA-registered installers belong to a unique bond and warranty scheme.

The Court of Appeal said that SPATA had not assumed legal responsibility to the Patchett's for the accuracy of the statements on the website without further enquiry which the website itself urged. Had the Patchett's asked for an information pack they would have learned that Crown was only an affiliate member and was not subject to checks and its customers would not have the benefit of the bond or warranty.

The case does indicate, however, that there is some potential for trade associations to be liable to end users of their members as a result of statements and representations made about their members, their codes and their warranty and bond schemes.

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