Fenwick Elliott
The construction law specialists

Issue 142 April 2012

Dispatch

Dispatch highlights some of the most important legal developments during the last month, relating to the building, engineering and energy sectors.

Good faith in long term contracts

Compass Group UK and Ireland Ltd (trading as Medirest) v Mid Essex Hospital Services NHS Trust [2012] EWHC 781 (QB)

The claim here related to a long-term facilities contract where clause 3.5 imposed a duty to cooperate in good faith:

"3.5 The Trust and the Contractor will co-operate with each other in good faith and will take all reasonable action as is necessary for the efficient transmission of information and instructions and to enable the Trust or...any Beneficiary to derive the full benefit of the Contract."

Medirest argued that this clause should be read as having imposed both a general obligation to cooperate in good faith and a more limited obligation to take all reasonable action as necessary for the two purposes contained in the clause, namely the efficient transmission of information and to enable the Trust to derive the full benefit of the contract. The Trust said that both obligations (i.e. to cooperate in good faith and to take all reasonable action) were qualified by the two purposes which followed. It was only therefore under a duty to cooperate in good faith in relation to those specific purposes. On either case, the parties had to take all reasonable action as necessary for the two purposes set out in the clause.

Mr. Justice Cranston, referring to the case of *Rainy Sky* v *Kookmin Bank* (see Issue 138) where the Supreme Court held that if a clause in a commercial contract is open to different interpretations, the court should generally adopt the interpretation which is closest to commercial common sense, indicated that had it had been necessary to choose, he would have held that there was a general obligation to cooperate in good faith. Here the parties had entered a long term contract for the delivery of services within a hospital, the performance of which, to work smoothly, required continuous and detailed cooperation at a number of levels. Therefore, it was highly likely that the parties intended that there should be a general obligation that they should cooperate in good faith, albeit that that obligation would be limited to the performance of the contract.

What really mattered in the dispute here was the content of the obligations contained in clause 3.5, to cooperate in good faith, and to take all reasonable action as was necessary, for the two purposes identified. The starting point in clause 3.5 was cooperation. The precise scope of the duty to cooperate would take its content from the circumstances and the nature of the contract concerned. In a long-term contract such as this the duty to cooperate necessarily required the parties to work together constantly, at all levels of the relationship, otherwise performance of the contract would inevitably be impaired.

Importantly, any lack of cooperation in the relationship in this context could have significant ramifications for patient well-being. The duty to cooperate necessarily encompassed the duty to work together to resolve the problems which would almost certainly occur from time to time in a long term contract of this nature. It also necessarily required the parties not to take unreasonable actions which might damage their working relationship. Here, the Judge said that the term good faith referred to how the parties were to conduct themselves in the course of its performance. Conduct which could be said to be committed in bad faith was clearly caught. Additionally, in its context, the term had an objective character and qualified how the duty to cooperate was to occur. This was the performance of a long term, complex contract, involving the provision of an important service to members of the public, the patients and visitors to the hospital. In deriving the full benefit of the contract under clause 3.5 for itself and the beneficiaries identified in the contract, the Trust was in a real sense pursuing a common purpose with Medirest of benefit to the public. To the Judge the objective standard of conduct demanded in this case of both parties primarily encompassed faithfulness to this common purpose.

Further, in addition to the duty to cooperate in good faith, clause 3.5 also contained the duty to take all reasonable action necessary for the efficient transmission of information and to enable the Trust to derive the full benefit of the contract. Those two purposes were broad. The Trust was not entitled to have regard merely to its own interest in securing the benefit of the contract; it was obliged as well to have regard to wider interests. This part of clause 3.5 imposed a broad obligation on the Trust to act reasonably in conducting the contract, in particular not taking unreasonable actions which might damage the relationship with Medirest and thus undermine the purpose of the contract. This obligation had an impact on the Trust's actions when it came to calculating service failure points and deductions. Clause 5.8 said this:

"The Trust… shall ascertain whether the Contractor's provision of the Services meets the performance criteria as specified … Where such performance criteria or standards have not been met …the Trust shall be entitled to levy payment deductions against the monthly amount of the Contract Price …the Trust may by notice to the Contractor award Service Failure Points depending on the performance of the Services as measured in accordance with the Service Level Specification."

In the Judge's view, the Trust could not overlook the obligations in clause 3.5. This included when calculating service failure points and deductions. On the facts here, Medirest accepted that its performance of the contract was such throughout this period that it had accumulated the number of service failure points necessary to terminate it.

Therefore, for example, the Trust was justified in serving a warning notice in late 2008. Throughout 2009 the Trust continued to have the right to terminate because Medirest's service failure points exceeded the contractual requisite of 1400. However, during the first part of 2009 the Trust's approach to the calculation of these points and deductions was in the view of the Judge "cavalier" and "absurd". This led the Judge to conclude that the Trust's actions during this period were in breach of its duties under clause 3.5. In broad terms these breaches revolved around both the manner of its calculations of service failure points and the failure to respond positively when Medirest challenged the calculations and tried to resolve the dispute. The breaches of contract on Medirest's part in 2008 were no justification for the Trust's breaches the following year. This meant that Medirest had been entitled to terminate the contract for what the Judge termed a material breach.

Case Update - bonds and the dangers of email

Golden Ocean Group Ltd v Salgaocar Mining & Anr [2012] EWCA Civ 265

We first reported on this case in Issue 131. The question before the courts related to whether a guarantee could be formed by a series of documents, largely emails, or whether it had to be in one document. The Court of Appeal endorsed the decision below. The requirement that the agreement must be in writing and signed by the guarantor was not there to ensure that the documentation was economical. The reason was to ensure that the parties knew exactly what had been promised and to avoid ambiguity.

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

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

Duties of contract administrators - bonds

Sweett (UK) Ltd v Michael Wright Homes Ltd [2012] EW Misc 3 (CC)

MWH engaged Sweett to act as the employer's agent and provide quantity surveying services for a housing development. It was an express term of Sweett's appointment that they would:

"Prepare contract documentation and arrange for such documents to be executed by the parties hereto"

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

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

Sweett argued that there was no absolute obligation to ensure that the contractor provided the bond. Its sole obligation was to take reasonable care to ensure that the performance bond was provided, and that by making numerous requests to the contractor they had successfully discharged this obligation.

HHJ Wildblood QC held that Sweett did not owe an absolute duty to ensure that the contractor provided the bond. He considered the definition of "arrange" and found that Sweet's obligation stopped short of the requirement to "ensure". Provided they put in place the necessary steps for the bond to be executed (which on the evidence it did) Sweet would effectively have discharged its duty to "arrange" under its appointment, and therefore any breach would be limited to the consultant's common law duty to exercise reasonable skill and care. Here the court noted the extensive steps that Sweet took in this case to try and secure the bond from the contractor. Here, Sweet made numerous attempts, including attending several meetings with both MWH and the contractor, and chased the contractor for updates on a regular basis.

This was sufficient to discharge the duty to "arrange" and to act with reasonable skill and care, by making numerous attempts to secure the bond.

Dispatch is produced monthly by Fenwick Elliott LLP, the leading specialist construction law firm in the UK, working with clients in the building, engineering and energy sectors throughout the world.

Dispatch is a newsletter and does not provide legal advice.

Edited by Jeremy Glover, Partner, Fenwick Elliott LLP
jglover@fenwickelliott.com
Fenwick Elliott LLP
Aldwych House
71-91 Aldwych
London WC2B 4HN

www.fenwickelliott.com