FENWICK ELLIOTT

The construction & energy law specialists

**Issue 206 - August 2017**

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

# Dispatch

## What is a defect?

### Imperial Chemical Industries Ltd v Merit Merrell Technology Ltd

[2017] EWHC 1763 (TCC)

ICI engaged MMT to carry out the manufacture, construction, installation and commissioning of steelworks at a new paint factory. The contract was an amended NEC3. The original contract value was £1.9million; as at the date of issue of the Claim Form, MMT had been paid £20.9 million. A number of issues arose over the quality of the welding and whether it was defective or not.

What is a defect? Clause 11.2 (5) defined Defect as including:

*"A part of the Works which is not in accordance with the Works Information..."*

Clause 40.4 states:

*"If a test of inspection shows that any work has a Defect, the Contractor corrects the Defect and the test or inspection is repeated"*

One of the key issues during the course of the litigation was the testing regime that MMT were required to comply with. The minutes of the post-tender meeting noted that visual inspection and 10% dye penetration were to be used and not radiography. Radiography was more expensive but was a more stringent testing regime. The experts agreed that a great many of what are described as "defects" in the welds can only be detected using radiography. The Judge was clear that this welding and inspection regime established by MMT prior to the commencement of the works was approved by ICI, and the Project Manager, before any physical welding commenced. However ICI maintained until the end of the liability trial that MMT was in breach of its contractual obligation by failing to perform such radiography.

The agreed testing regime meant that it was not possible to identify all the types of defect listed in the relevant British Standard. However, that was a direct consequence of the express agreement of the parties. ICI suggested that MMT should be held liable for welds contrary to those listed in Table 5 of the British Standard, even though it was agreed that radiography should not be a part of the testing regime contracted for by the parties. The Judge disagreed, saying that to hold MMT to a higher standard in terms of the quality of work required when ICI had expressly declined to contract with MMT for the radiographic testing necessary to be able to detect and assess compliance would be to re-write entirely the bargain struck by the parties in 2013. The Judge said:

*"It is illogical to consider something a defect for the purposes of the contract between ICI and MMT if the particular inspection method agreed between MMT and ICI is not fully effective for finding and assessing that flaw type. Defect is defined in the NEC3 contract terms as a part of the works not in accordance with the Works Information. Table 5 cannot, on any view, have formed part of the Works Information, Specification or any other contract document if the parties agreed that radiographic testing would not be done."*

## Repudiatory breach of contract

### Imperial Chemical Industries Ltd v Merit Merrell Technology Ltd

[2017] EWHC 1763 (TCC)

ICI alleged that MMT had committed a number of breaches that evinced an intention by MMT not to be bound by the terms of the contract; in other words these were repudiatory breaches. By a letter dated 17 February 2015, ICI wrote to MMT accepting what was said to be the repudiation of the contract by MMT, and thereby terminated MMT's employment under the contract. A party alleging repudiatory breach is not restricted to reliance on breaches known about at the date of the acceptance of the purported repudiation. However, here, the Judge did not consider that any of the claims were made out.

For example, determining the number or proportion of welds that were defective when considered against the agreed contract terms was difficult for ICI because the contemporaneous reports proceeded on the basis that the specification against which the welds were to be measured was that contained in the British Standard, testing performed by radiography. They were not comparing the welds against the contractual standard agreed with MMT. Therefore the determination of "defects" was flawed. This was not a repudiatory breach. In fact the Judge commented that:

*"This attempt to particularise repudiatory breaches by MMT appears as though someone has simply trawled through the entirety of the project correspondence, and any passing reference to any matter (such as the isolated references to the welder working on different welds to that for which he was qualified) has been elevated to the status of being a repudiatory breach or breaches. The experts opined on this – and qualification is important—but the factual evidence is that this was simply not an issue at the time. ICI seek to elevate it to a greater importance than it merits to bolster a thin case on repudiatory breach by MMT."*

As the Judge dismissed all the alleged breaches relied upon by ICI, this meant that the 17 February 2015 letter was not the exercise of a contractual right to terminate, but was itself a repudiation of the contract by ICI. Here, the Judge also referred to a request made by ICI, also on 17 February 2015, for the production of documents. The Judge noted that this request was "couched in an unrealistically short time frame" such that it could not possibly have been complied with. The letter was received at 2.40 p.m. and compliance expected by 5 p m. MMT could not be considered to be in breach of the contract term by failing to comply with the request because it simply would not have been possible for MMT to have produced the documents within the period of time stated. The word "forthwith" has to be considered in the light of all the circumstances at the time. MMT was entitled to a reasonable period of time, first to take legal advice, and then to prepare and copy the documents.

Accordingly, ICI was itself in repudiatory breach of contract by instructing MMT to leave site on 17 February 2015.

## Adjudication: final and binding?

### Imperial Chemical Industries Ltd v Merit Merrell Technology Ltd

[2017] EWHC 1763 (TCC)

There had been a number of adjudications, some involving payment applications. Mr Justice Fraser commented that:

*"As a term for this type of dispute or adjudication, in my judgment the phrase '"smash and grab"' is best avoided. The phrase has clearly pejorative overtones ... If employers or third party certifiers fail to comply with those legal requirements, then the party seeking payment (usually the contractor) becomes entitled to the sum (as an interim payment) for which application has been made. To describe an attempt, or the adjudication itself, by a party to enforce these legal rights as a '"smash and grab"' entirely misses the point. An adjudicator in such a dispute has a more straightforward task than in other adjudications on other more complicated facts – he or she will usually only need to consider the timings and contents of certain notices.""*

If, as here, a contract comes to an end through repudiation, whilst further performance of the contract by both parties comes to an end, the existing rights and obligations the parties have, as at the time the contract comes to an end, remain. This meant that here, if ICI had a right as of 17 February 2015 to recover overpayments under the contract, that right remained in being even though it was ICI who repudiated the contract. MMT suggested that the most that interim assessments could be said to be was a definitive or final valuation of the works for all purposes at that point in the project. This was potentially significant as the total sum paid to MMT as at the date of this trial included sums paid pursuant to two adjudication decisions. MMT suggested that the sums claimed in the interim application in question had therefore been subject to "a judgment on the merits"

The Judge did not consider this to be strictly correct. The decision in question was based upon the lack of pay less notices. They were then subject to enforcement proceedings which were, very late in the day, conceded and the amount due was paid. This was not a judgment and did not change the character of the adjudicator's decision to one that was finally binding, rather than binding on an interim basis. The Judge noted that clause 50.5 made it clear that: *"The Project Manager corrects any wrongly assessed amount due in a later payment certificate."* Further a review of recent cases showed that the value of the works remained something that could be challenged. In other words, the value of the works executed was not definitely determined by the figure in the interim assessment (or an adjudicator's decision on that interim assessment). The Judge further considered that this was not something that could be: *"sensibly be argued otherwise,given the nature of adjudication."* This meant that notwithstanding the adjudicator's earlier decisions, the Judge concluded that:

*"the amount to which the contractor is entitled as final payment for the works is not definitively decided as the figure in the most recent interim assessment."*

## Expert and witness evidence

### Imperial Chemical Industries Ltd v Merit Merrell Technology Ltd

[2017] EWHC 1763 (TCC)

During the course of the judgment, Mr Justice Fraser made a number of comments about the importance of witness and expert evidence at every stage of the litigation process not just at trial. He noted that: "*It should go without saying that witness statements to the court should be factually accurate in any event. This is as important for those served for interlocutory applications*."

With witnesses of fact, care must be taken not to "ignore important aspects of the factual background" that do not match your case.

Parties should also take care not to remove potentially important evidence. Here there was reference in the evidence to ICI, at least initially, having kept hold of the allegedly defective welds. However it was found in January 2017, that all the samples had been scrapped. Although non-destructive testing reports for some of the welds survived, the reports alone, were not the same as enabling the experts to actually physically inspect the welds in question. Here, it was ICI's case that the quality of the welding by MMT was below the necessary standard. The lack of physical evidence could not but adversely affect the strength of the case so advanced. The Judge noted that:

*"Such destruction of physical evidence in any event, but particularly when the question of the quality of the welds is such a contentious issue between the parties, should not have occurred and I am greatly troubled by it."*

As for expert reports, care must be taken when experts add qualifications to a joint report. Here this happened when two of the experts added paragraphs to the already agreed joint statement on the day it was signed. However their opposite number did not have any opportunity for discussion or review. The Judge noted that this was not an appropriate way of attempting to bolster, or add to the written evidence, after that written evidence had already been exchanged. This was: "*not the function of a joint statement by experts."*

Experts should also take care not simply to accept one party's case. There was another issue over the total number of weld reports prepared by a testing company. There were around 1,800 in total, but the expert was only provided with 412. This meant the expert was using a sample far smaller than the one available in disclosure. The expert asked for the complete sample, but was not provided with it. Whilst the Judge was critical of the failure to provide all the reports, he was equally critical of the expert who *"glossed over this absence of data, even though he knew it existed and had specifically requested that it be provided*." This was not the action of an impartial independent expert.

Further, the expert attempted to maintain his original conclusion, based on the smaller survey. The lead the Judge to conclude that the expert in question had lost the degree of independence and impartiality, expected of all experts. Here the expert became a "cheerleader" for the party that was instructing him. An expert must have regard to the case being put forward by the other side. Where there are matters for a court to resolve, the expert should identify this in their report. The Judge noted that:

*"An expert's role is not to decide issues of fact themselves, and choose what facts to believe and what not to believe."*

***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**
jglover@fenwickelliott.com
Tel: + 44 (0)20 7421 1986

**Fenwick Elliott LLP**
Aldwych House
71 - 91 Aldwych
London WC2B 4HN

**www.fenwickelliott.com**