Fenwick Elliott
The construction law specialists

Issue 124 October 2010

Dispatch

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

Liquidated damages - guarantees

Azimut-Benetti SpA v Healey
[2010] EWHC 2234 (Comm)

Azimut build luxury yachts. On 25 September 2008, Azimut and Shoreacres Ltd (a company wholly owned by Mr Healey) entered into a contract whereby Azimut agreed to construct a 60 metre yacht for €38 million payable in instalments. The delivery date was 30 November 2011. Mr Healey provided a personal guarantee. Shoreacres paid a deposit of €0.5 million but failed to pay the first instalment of 10% of the price, which was due on 17 October 2008. Azimut eventually terminated the contract on 22 January 2010.

Clause 16.3 provided that if Azimut lawfully terminated the contract, it would be entitled to retain or recover 20% of the price by way of liquidated damages as compensation for its estimated losses. This clause also required Azimut to refund the balance of instalments over and above the 20% amount. Azimut sought summary judgment against Mr Healey. Mr Healey argued that the liquidated damages clause in the contract with Shoreacres was not a genuine pre-estimate of loss but a penalty, so that there was no liability on which the guarantee could fasten.

Whilst negotiations took place for yacht in question, the advisors retained for Shoreacres were independently retained for the purchaser of a similar yacht. In the context of that yacht, there was evidence before the Court of discussions regarding the commercial reasoning for clause 16.3. There was no evidence of discussions regarding this clause in relation to Mr Healey's yacht, but his/Shoreacres' advisors would have been aware of the discussions in relation to the other contract. And so, the parties accepted before the court that this evidence was admissible so far as it went to the reasons the parties had for agreeing the clause in question.

Mr Justice Blair held that Azimut was entitled to summary judgment for €7.1 million, being 20% of the contract price less €0.5 million paid by way of deposit, on the basis that it was not arguable that clause 16.3 was a penalty. At the time the contract was entered into the dominant purpose of clause 16.3 was not to deter Shoreacres from breach. The clause was commercially justifiable as providing a balance between the parties upon lawful termination by Azimut. Even though the Judge did not have to decide the issue given his conclusion that clause 16.3 was not a penalty, in an obiter comment he rejected Azimut's alternative argument that Mr Healey would have been liable under the guarantee even if the liquidated damages clause had been held to be a penalty. Such an outcome would be against public policy and in any event, since the guarantee was limited to the obligations of Shoreacres, if Shoreacres had no obligation under the contract, Mr Healey would have no obligation under the guarantee. Clause 16.3 was more than just a bare liquidated damages clause as it served the further commercial purpose of returning the balance of instalments paid by Shoreacres upon termination. The balancing of commercial considerations for Shoreacres when entering into the contract was that upon termination it would have the advantage of an immediate refund of the balance of instalments already paid which totalled more than 20% of the price. The Judge concluded that both parties had the benefit of expert representation in the conclusion of the contract. The terms, including the liquidated damages clause, were freely entered into:

"As the authorities referred to...show, in a commercial contract of this kind, what the parties have agreed should normally be upheld."

Insurance & disclosure - avoiding the policy

Travelers Insurance Company Ltd v Countrywide Surveyors Ltd
[2010] EWHC 2455 (TCC)

On 25 May 2008 Countrywide took out a professional indemnity policy of insurance. Travelers was the lead underwriter. It appeared that hundreds of potentially fraudulent valuations may have been carried out by certain employees. As a result there was a possibility that Travelers would seek to avoid the policy for misrepresentation and/or non-disclosure. Accordingly, Travelers sought disclosure of documents from Countywide in order to assess whether or not to seek to avoid the policy. The documents were relevant to the extent to which the possibility of fraud as opposed to allegations of incompetence was known to Countrywide at the time the policy was agreed. They also related to the circumstances surrounding the individual's dismissal.

In response to threats of an application for pre-action disclosure pursuant to CPR 31.16. Countrywide provided a large number of documents. However, Travelers maintained that there were more. Countrywide argued that the Court did not have the necessary jurisdiction to make the order sought, because the power to order pre-action disclosure does not extend to a situation where the dispute between the parties will be determined via arbitration. The Judge accepted that the overall purpose of the exclusion provision in the policy was to ensure that the policy was not avoided because of an inadvertent misrepresentation or non-disclosure. However, this condition specifically included an arbitration agreement in contrast with the general provisions of the policy which stated that all other disputes under the policy will be dealt with in the courts. Therefore Mr Justice Coulson held that the arbitration agreement had to apply and would thereby deprive the Court of the power to make an order for pre-action disclosure.

The Judge refused the application with "a certain amount of regret" and it should be noted that had the arbitration clause not applied, the outcome would have been different. The documents sought, particularly those relating to the decision as to what information to provide to Travelers and what information not to provide, would be disclosable on standard disclosure if and when this dispute came before a tribunal. The early provision of that documentation would plainly narrow the issues and reduce costs and there was a real chance that, if all the information sought was provided, Travelers would take the view that there had not been fraudulent intent, so that the issue would never even arise. In any event, the early production of information would allow Travelers to make an informed decision as soon as possible, on the basis of the fullest available information. And that result would have been in everybody's interests.

Arbitration - failure to identify the seat of the arbitration

Chalbury McCouat International Ltd v P.G. Foils Ltd

[2010] EWHC 2050 (TCC)

Chalbury McCouat, an English company with its principal place of business in England, entered into a contract on 8 February 2008 ('the contract') with PG Foils Ltd to dismantle its manufacturing plant in Vaassen in the Netherlands. PG Foils Ltd is an Indian company operating in Rajasthan and the parties had entered into a further, separate agreement by which the plant would then be reassembled in India. A dispute arose in relation to the payment under the contract. Chalbury McCouat attempted to invoke the arbitration clause in the contract which stated that the dispute was to be referred to "arbitration as per prevailing laws of European Union in the Europe".

However, PG Foils Ltd withheld its consent to appoint the arbitral tribunal. It alleged that since the performance of the contract was to be completed in India and that the contract was signed and executed in the India, either an "Arbitral Tribunal in India" should be appointed, or alternatively the provisions of the Indian Arbitration and Conciliation Act 1996 should apply. Chalbury McCouat subsequently issued an arbitration claim form, obtained permission to serve the claim form outside the jurisdiction and then applied to the court to exercise its powers under section 18 of the 1996 Act to appoint the arbitral tribunal.

The dispute resolution clause within the parties' agreement was clear that failing resolution by discussion, the dispute should be referred to arbitration. However, the arbitration clause was silent as to the seat of the arbitration. Accordingly, in order for the Mr Justice Ramsey to appoint the arbitral tribunal by virtue of section 18 of the 1996 Act, he first had to consider whether or not there was a connection with England and Wales, in accordance with section 2(4) of the 1996 Act. Mr Justice Ramsey referred to the Departmental Advisory Committee's Report of January 1997 and the Court of Appeal's decision in *International Tank & Pipe SAK v Kuwait Aviation Fuelling Co KSC (1975)* and found there will be a sufficient connection with England and Wales if the proper law of the contract is English law. However, it this case, there was no express choice of law stating what law (lex causae) was to be applied to the substance of the dispute.

As the law to be applied to the procedure of the arbitration (lex fori) was the laws of European Union, the judge found that this suggested that the proper law to be applied to the dispute should be determined under the law of the European Union, which are set out in the Rome Convention. In accordance with Article 4 of the Rome Convention, the performance of the work of dismantling the plant was to be carried out by Chalbury McCouat, an English company with its principal place of business in England. On this basis, Mr Justice Ramsey therefore considered that the contract was most closely connected with England and the arbitral tribunal were likely to find that the proper law is English law.

So far as the seat of the arbitration is concerned, he found that the reference to "arbitration as per prevailing laws of European Union in the Europe" means that the seat of arbitration was likely to be Europe, possibly England and unlikely to be India. Furthermore, the fact that payment under the Contract was made in England was further evidence of a connection with England. Accordingly, Mr Justice Ramsey held that because of the connection with England, it was appropriate for the Court to exercise its powers under section 18 of the 1996 Act. He ordered that the President (or in his absence the Vice-President) of the London Court of International Arbitration (LCIA) make the necessary appointment of a sole arbitrator.

In this case, the parties' resolution of their dispute was ultimately prolonged by the fact that their contract had failed to identify the choice of law to be applied to the substance of the dispute, as well as failed to identify the seat of the arbitration. This resulted in further disagreements regarding the appointment of the arbitral tribunal and potentially further costs. This exemplifies the importance of discussing and agreeing your dispute resolution clause at the outset of any project. In addition, this case is a further demonstration of the English court's support of the arbitral process. Though there had been some difficulty in the interpretation of the parties' contract, Mr Justice Ramsey nevertheless stated:

"When parties have agreed to arbitrate then I consider that the court should strive to give effect to that intention and should seek to support the arbitral process."

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.

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