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Dispatch

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

Guarantee or On-Demand Bond?

Wuhan Guoyu Logistics Group Co Ltd and another v Emporiki Bank of Greece SA
[2012] EWHC 1715 (Comm)

The claimants jointly operated a shipyard in China ("the Seller") and entered into a shipbuilding contract for the construction of a bulk carrier. The contract was later novated to two other companies ("the Buyer"). The contract price for the vessel was payable in five instalments, with the second instalment to be paid on receipt by the buyer of a "Refund Guarantee" issued by the claimant's bank, together with a certificate of the cutting of the first 300m steel plate of the vessel. In turn, the Buyer was to give a "Payment Guarantee" in respect of the second instalment. On 14 December 2007 the defendant Bank issued a Payment Guarantee providing finance to the Buyer and to which the Buyer had assigned all claims under the shipbuilding contract and the refund guarantee.

A dispute arose and the Buyer did not pay the second instalment. The Seller made a claim under the Payment Guarantee on 22 June 2011, arguing that it was a performance bond which was due on written demand, regardless of whether the underlying payment was due. The Seller claimed summary judgment for the principal and interest. Conversely, the Bank said that the instrument was properly called a guarantee, therefore its liability, as guarantor, was contingent on an underlying obligation. The Bank argued that its liability could not be decided summarily as there was a genuine dispute as to whether the second instalment was in fact due.

The relevant clauses of the Payment Guarantee provided:

"(1)… We hereby irrevocably absolutely and unconditionally guarantee, as the primary obligor and not merely as the surety, the due and punctual payment by the BUYER of the 2nd instalment of the Contract Price… as specified in (2) below.

(2) The instalment guaranteed hereunder pursuant to the terms of the Shipbuilding Contract, comprises the 2nd instalment… payable by the BUYER within five New York banking days after completion of cutting of the first 300 MT of steel plate…

(4) In the event that the BUYER fails to punctually pay the second instalment guaranteed hereunder…then, upon receipt by us of your first written demand stating that the BUYER has been in default of the payment obligation for twenty (20) days… we shall immediately pay to *you… the unpaid 2nd Instalment…"*

Clarke J refused to grant summary judgment in favour of the Seller on the basis that the Bank had an arguable case that the Payment Guarantee was a guarantee and not a performance bond.

The Judge noted that the Payment Guarantee was continuously referred to as a guarantee, and used the classic language of a guarantee. The Bank's undertaking under the Payment Guarantee was the liability of a guarantor in respect of the second instalment, and not simply an agreement to pay on demand the second instalment in the event that the Buyer failed to make payment. The Payment Guarantee also clearly described the circumstances in which the Bank should make payment under clause 2. This included a requirement that notice of the cutting of the steel be counter-signed by the beneficiary of the guarantee, which acted as a condition precedent to payment.

Despite containing some features of a demand bond, including a provision in clause 4 for immediate payment on "first written demand", and repeated references to the guarantor as "a primary obligor", in the context of the rest of the Payment Guarantee Clarke J held that this was not inconsistent with it being construed as a guarantee. Clarke J relied on the decision in *Carey Added Value SL v Grupo Urvasco SA* [2010] EWHC 1905 (Comm), where it was decided that the wording "primary obligor" was not a decisive indication that an instrument was a demand bond.

Therefore the cumulative effect of the guarantee's clauses was that the primary obligation undertaken by the Bank was an obligation to pay the sum actually due under the shipbuilding contract. Only when the underlying sum was due, was payment due under the Payment Guarantee.

Agreements to negotiate in good faith

Charles Shaker v Vistajet Group Holding SA
[2012] EWHC 1329 (Comm)

This case concerned an application for summary judgment on a claim for the return of a deposit of $3.55m paid by Shaker to Vistajet pursuant to the terms of a Letter of Intent in respect of a potential transaction concerning the purchase, operation and repurchase of an aircraft. Under the terms of the LOI, Shaker agreed to *"proceed in good faith and to use reasonable endeavours to agree, execute and deliver"* certain documents by a cut off date. Vistajet was to refund the deposit within five days of the cut off date where the *"seller and buyer, despite the exercise of their good faith and reasonable endeavours, failed to reach agreement…"* Vistajet argued that since Shaker had not proceeded in good faith or used reasonable endeavours to agree the relevant transaction documents, he was not entitled to the return of the deposit.

Teare J referred to the recent decision in *Barbudev v Eurocom* [2012] EWCA Civ 548 as authority for the principle that agreements to use reasonable endeavours to agree or to negotiate in good faith are unenforceable.

He stated that the "*reason for such unenforceability is that there are no objective criteria by which the court can decide whether a party has acted unreasonably and that a duty to negotiate in good faith is unworkable because it is inherently inconsistent with the position of a negotiating party*". The Judge expressed some doubt as to whether under the terms of the LOI, the exercise of good faith and reasonable endeavours was a condition precedent to the return of Shaker's deposit. He concluded that such a condition precedent would nevertheless be unenforceable for the same reasons and ordered the return of the deposit.

Extension of time and global claims

Walter Lilly & Company Ltd v Mackay and DMW Developments

[2012] EWHC 1773 (TCC)

Walter Lilly was engaged by DMW in 2004 as a main contractor under a JCT Standard form of Building Contract with bespoke amendments to build three houses at 1, 2 and 3 Boltons Place, Earls Court. Mr and Mrs Mackay were to occupy number 3 on completion. Mr Mackay (together with Mr Daniel and Mr West, who were to occupy numbers 2 and 3) formed DMW as the corporate vehicle through which the development would be carried out. Little, if any of the design had been completed prior to the involvement of WLC, as a result of which the project suffered from considerable delay.

Upon commencement of the project, DMW and WLC agreed to split the building contract in three so that there would be a separate contract for each plot. A deed of variation dated 23 December 2004 was signed to this effect. Throughout the project period WLC had sought, and was granted, extensions of time on numerous occasions by the first architect under the building contract. DMW eventually changed architect and at the date of practical completion (deemed by the court to have occurred on 7 July 2008) DMW withheld liquidated damages for late completion.

WLC argued that it was entitled to an extension of time for the whole period of delay. DMW said that WLC was responsible for the delays. Akenhead J notably distinguished between a prospective assessment of delay by the architect before practical completion occurs and a retrospective analysis by a court, arbitrator or the architect after practical completion. Following this approach, the judge found that the court must use its knowledge of events as provided by witness and expert evidence, and on the balance of probabilities should determine what delay was actually caused by relevant events. Mr Justice Akenhead considered a number of English authorities on concurrent delay including *Henry Boot Construction (UK) Ltd v Malmaison Hotel (Manchester) Ltd* [1999] and the more recent decision in *Adyard Abu Dhabi v SD Marine* [2011]. He determined that:

"where there is an extension of time clause such as that agreed upon in this case, and delay is caused by two or more effective causes, one of which entitles the contractor to an extension of time as being a relevant event, the contractor is entitled to a full extension of time".

In reaching his conclusion, while recognising the judgment as *"persuasive"*, the Judge notably rejected the approach taken by the Scottish court in *City Inn Ltd v Shepherd Construction Ltd* [2010] as "*being inapplicable in this jurisdiction*".

The Judge therefore held that WLC was entitled to the full extension of time claimed.

WLC and DMW had agreed that in order to claim loss and expense under the building contract, WLC had to make a timely application and provide details of the loss and expense claimed. In relation to loss and expense generally, following the guidance in *London Borough of Merton v Stanley Hugh Leach* [1985], the court found that the requirement to provide "*reasonably necessary*" detail in accordance with JCT wording does not in effect give rise to an obligation on part of a contractor to provide details that prove its claim beyond all reasonable doubt. Information provided in support of a loss and expense claim needs to be sufficient to satisfy a court or arbitrator that the contractor has on the balance of probabilities incurred such loss as a result of a relevant event.

DMW argued that WLC's claims amounted to a global claim which should, on the facts, fail in its entirety. Upon a thorough review of the relevant authorities, Mr Justice Akenhead observed that when claiming costs a contractor has to prove its claim as a matter of fact and has to demonstrate on the balance of probabilities that (1) events have happened which entitle it to loss and expense; (2) that those delays caused delay and/or disruption and (3) that such delay or disruption caused it to incur loss and/or expense/damage. The judge further stated that "*there is nothing in principle "wrong" with a "total" or "global" cost claim*", however, "*there are added evidential difficulties… which a claimant contractor has to overcome. It will generally have to establish (on a balance of probabilities) that the loss which it has incurred (namely the difference between what it has cost the contractor and what it has been paid) would not have been incurred in any event…*"

Significantly, the court held that a global claim will not automatically fail on the basis of a single issue not properly pleaded or proved, or which is shown to be the fault of the contractor. In such circumstances, following the approach in *John Doyle Construction Ltd v Laing Management (Scotland) Ltd* [2004], the Judge clarified that the claim would simply be reduced by the value of the event or series of events in question.

The court, however, concluded that WLC's claim was not a "global" claim and added that even if WLC had in fact made a global claim, the latter had demonstrated that its original preliminaries prices were realistic and set at a level which, if the events referred to had not arisen, would not have led to the losses it ultimately suffered.

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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