Hurley Palmer Flatt Ltd v Barclays Bank Plc [2014] EWHC 3042 (TCC); TCC; Ramsey J

In 2008, Barclays PLC (B PLC) and Hurley Palmer Flatt Ltd (HPF) entered into an appointment (the Appointment) for HPF to provide mechanical and electrical engineering design services in relation to a new data hall at a data centre. Disputes arose as a result of problems with the chilled water system which led to a claim against HPF valued at £4 million.

Clause 14.3 of the Appointment entitled any ‘Affiliate’ to enforce the terms of the Appointment ‘as Client’, provided that HPF could ‘rely on the equivalent defences in respect of such liability which it has against [B PLC]’. Barclays Bank PLC (BB PLC) fell within the definition of ‘Affiliates’.

The Appointment excluded the Contracts (Rights of Third Parties) Act 1999 (CROTPA) ‘unless expressly stated otherwise’. Clause 14.2 of the Appointment also stated that save for cl 14.3 and obligations in relation to collateral warranties, nothing therein conferred ‘any benefit or right to enforce any terms of [the Appointment]’ on third parties.

Part 1 of the Scheme for Construction Contracts (England and Wales) Regulations 1998 (the Scheme) in relation to adjudication was incorporated into the Appointment, which also stated that the decision of any adjudicator would be binding upon the parties, unless and until determined by legal proceedings.

In August 2014, BB PLC issued a notice of adjudication to HPF regarding damages arising from the issues with the chilled water system. HPF issued CPR Pt 8 proceedings seeking a declaration that BB PLC was not entitled to commence adjudication and that the adjudicator did not have jurisdiction.

The key question was whether the rights given to BB PLC included the right to adjudicate. HPF argued that BB PLC had no such right, on the basis that s 8, CROTPA states that a third party to an arbitration agreement is treated as a party to that arbitration agreement, but there is no such provision in relation to adjudication. BB PLC argued that s 1(4), CROTPA states that a third party’s right of enforcement is ‘subject to and in accordance with any other relevant terms of the contract’ and therefore BB PLC’s rights to enforce the Appointment were subject to the right to adjudicate.

Decision
Ramsey J held that BB PLC was not entitled to commence adjudication proceedings against HPF and that the adjudicator did not have jurisdiction to determine this claim.

The effect of cl 14.3 and the exclusions of other third party rights referred to above, was held to be that cl 14.3 contained the ‘full scope’ of a third party’s rights to enforce the Appointment. The words ‘such liability’ in cl 14.3 indicated that cl 14.3 covered the terms of the Appointment in relation to liability, but not ‘procedural rights’.

As regards BB PLC’s argument in relation to CROTPA, s 1(4), the court considered this to be insufficient to give a third party a right to adjudicate, given that s 8, CROTPA expressly entitled a third party to enforce an arbitration agreement but did not refer to adjudication. Adjudication, unlike arbitration, is not mandatory but voluntary and the Explanatory Notes to s 8, CROTPA expressly stated that in the absence of s 8 an arbitration agreement would not apply between the parties to a contract and the third party.

It was also significant that the Appointment referred to the Scheme, which states that a party to a construction contract can refer disputes to adjudication. BB PLC was not a party to the Appointment.
Significance
Any construction contract granting a third party rights to rely upon that contract should be drafted very carefully if that third party requires the right to adjudicate when enforcing its rights. The clause granting the third party any rights, any exclusion of other third party rights and the adjudication provisions should all be considered.

This case can be contrasted with Parkwood v Laing O Rourke [2013] EWHC 2665 (TCC), in which it was held that in some circumstances a collateral warranty will be a ‘construction contract’, giving the beneficiary the right to adjudicate. Whilst both collateral warranties and any rights granted under CROTPA should be considered on a case by case basis, these cases could further encourage third parties to require a collateral warranty rather than rights under CROTPA.

Unaoil Ltd v Leighton Offshore Pte Ltd [2014] EWHC 2965 (Comm); Comm Ct; Eder J

Leighton Offshore PTE Ltd (Leighton) and Unaoil Ltd (Unaoil) entered into a Memorandum of Agreement (MOA) in 2010, pursuant to which Leighton would tender for works as part of the Iraq Crude Oil Export Facility Reconstruction Project (the Project) and appoint Unaoil as its sub-contractor.

The MOA stated that Unaoil would be paid an all-inclusive price of $75 million. In addition, art 8 of the MOA gave Unaoil the right to ‘liquidated damages in the total amount of USD 40,000,000’ if Leighton was awarded the contract for the Project but did not comply with the MOA and award the sub-contract to Unaoil. The MOA also stated:

‘after careful consideration by the Parties, the Parties agree such amount is proportionate in all respects and is a genuine pre-estimate of the loss that [Unaoil] would incur’.

The MOA was subsequently amended in March and April 2011, such that the price payable to Unaoil was reduced to $55 million. Leighton entered into the contract for the Project in October 2011, but did not enter into a sub-contract with Unaoil.

Unaoil commenced proceedings against Leighton in April 2012, seeking to recover advanced payments which it alleged were due under the MOA, liquidated damages under art 8 of the MOA and damages as a result of Leighton’s repudiatory breach of contract.

For the purpose of this summary we will focus on Unaoil’s claim for liquidated damages. Leighton argued that art 8 was a ‘penalty clause’ and therefore unenforceable, whereas Unaoil submitted that the $40 million figure was not ‘extravagant and unconscionable’ and that despite the reduction in the contract price, there was no evidence that Unaoil’s intention in relation to the liquidated damages changed as a result of the variation.

Decision
Eder J rejected Unaoil’s claim for liquidated damages but awarded Unaoil $12,577,500 in respect of the advanced payment.

In rejecting Unaoil’s claim for liquidated damages, the court held that, even if the liquidated damages were a genuine pre-estimate of loss at the time of the original contract, the relevant date at which this should be considered if a contract is amended, is the date of the amended contract:

‘[O]nce the contract price was reduced, it was, on any objective view, “extravagant and unconscionable with a predominant function of deterrence” without any other commercial justification for the clause.’

Following the reduction of the contract price to $55 million the liquidated damages were:

‘manifestly … no longer … a genuine pre-estimate of the likely loss by a very significant margin’.

Significance
This decision emphasises that any liquidated damages should be considered very carefully, so as to ensure that they are not deemed to be a ‘penalty’. Those who wish to rely upon liquidated damages should ensure that they can demonstrate that they are not ‘extraordinary and unconscionable’, but are a genuine pre-estimate of the loss. This applies both when a contract is entered into and following any subsequent amendments, particularly if those amendments reduce the contract sum. If the liquidated damages are unchanged following such a reduction, this could give the contractor the right to argue that the clause is a ‘penalty’ and invalid and therefore cannot be enforced. CL