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High Court finds Brexit did not frustrate lease – impact on construction contracts

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The European Medicines Agency (EMA) has lost a High Court challenge brought by the Canary Wharf Group (CW) over the potential termination of its 25-year office lease. The decision will be of interest to those reviewing and negotiating construction contracts in light of Brexit.

Background

A contract may be discharged on the ground of frustration when the law recognises that without default of either party a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract.

In 2014, the EMA entered into an underlease of part of Churchill Place, Canary Wharf for a term of 25 years. CW were the landlords and management company for the estate. In August 2017, the EMA wrote to CW stating that:

> "*Having considered the position under English law, we have decided to inform you that if and when Brexit occurs, we will be treating that event as a frustration of the Lease.*"

CW took the view that the commercial uncertainty created for CW and their lenders by this contention required early resolution. CW sought a declaration that:

> "*. . . the withdrawal of the United Kingdom from the European Union and/or the relocation of the [EMA] (whether inside or outside of the United Kingdom) will not cause [the Lease] to be frustrated and that the [EMA] will continue to be bound by all of its covenants and obligations in the Lease and all related documents including (but not limited to) payment of the full rents under the Lease throughout the Term of the Lease unless released by law upon a lawful assignment of the Lease properly made in accordance with its terms . . .*"

Decision

The EMA relied on two main arguments: frustration of common purpose and frustration by supervening illegality:

- **Frustration by supervening illegality** – The EMA argued that after withdrawal of the UK from the EU, it would no longer be lawful for the EMA to pay rent to CW pursuant to the lease. The payment of rent would be unlawful because the EMA would, in paying rent, be acting ultra vires or without capacity.

  The Court rejected this argument on the basis that the EMA has the capacity, post the withdrawal of the UK from the EU, to continue to use and/or dispose of the premises and that it continues to have the capacity to pay rent (and perform its continuing obligations) under the lease.

- **Frustration of common purpose** – Alternatively, the EMA argued that the lease should be discharged due to frustration of a common purpose.

  The Court found that there was no common purpose between the parties. The EMA was focussed on bespoke premises, with the greatest

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flexibility as to term and the lowest rent. CW was focussed on long-term cash flow, at the highest rate, and was prepared to allow the EMA its say in the building's configuration, provided that this was not adverse to CW's interests.

The Court concluded the lease will not be frustrated on the withdrawal of the UK from the EU. This is neither a case of frustration by supervening illegality nor one of frustration of common purpose. The lease will not be discharged by frustration on the UK's transition from Member State of the EU to third country nor does the EMA's shift of headquarters from London to Amsterdam constitute a frustrating event. The EMA remains obliged to perform its obligations under the lease.

A copy of the full judgment is available at: https://www.bailii.org/ew/cases/EWHC/Ch/2019/335.pdf

Impact on Construction Contracts

The judgment will be read with interest by those reviewing and negotiating construction contracts in light of Brexit.

Brexit-related events may have a significant commercial impact. Parties should consider expressly providing for situations in which their ability to perform, or their costs of performing the contract could be affected by Brexit.

A "Brexit clause" can be included in a contract to seek to trigger a change in the parties' rights and obligations as a result of a pre-defined event occurring. There are two main types of Brexit clauses to consider:

- **Specific event – specified consequence** – If a specific event occurs (for example, there is a change in an exchange rate or a delay), then a specified consequences follows (using the same examples, a price adjustment or an extension of time).
- **Trigger – renegotiation – termination** – Where a trigger occurs (for example, a change in regulatory requirements), the affected party can request to renegotiate the contact and, if no deal can be reached, the affected party can terminate.

When reviewing existing contracts, consider whether the following might be of assistance:

- **Force majeure** – typically excuses one or both parties from performance of the contract in some way following the occurrence of certain events (note that standard force majeure wording is unlikely to assist).
- **Compliance with laws** – requires the parties to comply with applicable law (usually at either the date the contract is entered into or as applicable from time to time). For example, see Option X2 in the NEC forms, which provides that a change in law will be a compensation event.
- **Economic hardship** – which party should bear the burden of increases in the costs of supply, exchange rates, labour etc.
- **Change control** – setting out the procedure to follow when either party wishes to change the contract.
- **Termination** – the right to terminate the contract in certain specific circumstances. Clients, and funders, are likely to insist on a termination clause to allow them to exit the project "at will", to deal with circumstances if the project no longer becomes viable – this is the standard position in the public sector.

If you have any Brexit or contract queries, please do not hesitate to contact:

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