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CONTRACTS: WHAT'S HOT, WHAT'S NOT

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CONTRACTS: WHAT'S HOT, WHAT'S NOT



Chris Bates
Partner, Digital Economy Transactions

Christopher.Bates@ashurst.com
+44 (0)20 7859 2388

Topics for this session

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INDEMNITIES:

recognising them, and interpreting time limits

2

EXCLUSION CLAUSES:

indirect and consequential loss, and financial caps

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BREACH OF CONTRACT:

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"WILFUL"



INDEMNITIES:

Recognising them, and
interpreting time limits

1

Indemnities: how to recognise them

AXA SA –V- GENWORTH FINANCIAL INTERNATIONAL HOLDINGS, INC [2019] EWHC 3376 (COMM)

Was this clause, in a SPA, an indemnity?

"The Sellers hereby covenant to the Purchaser and each Target Group Company that they will pay to the Purchaser or such Target Group Company on demand an amount equal to:

a. ...90% of all Relevant Distributor Mis-selling Losses; and

b. ...90% of [other losses]..."

The obligation was to continue until specified events occurred, which ultimately did not happen – with expensive consequences.

Indemnities: how to recognise them

AXA SA –V- GENWORTH FINANCIAL INTERNATIONAL HOLDINGS, INC [2019] EWHC 3376 (COMM)

Approach with an open mind and no preconceptions

Construe the clause in accordance with its language, the rest of the document, and the admissible factual matrix

Fact of a “bad bargain” is irrelevant

Wood –v- Capita Insurance Services Ltd
[2017] AC 1173:

- What is the objective meaning of the language chosen by the parties?
- A unitary exercise involving an iterative process
- Language is balanced against other factors, such as the nature and formality of the contract, and the quality of drafting
- “Textualism and contextualism are not competing paradigms”

The Antaios [1985] A.C.191 (Lord Diplock):
“business commonsense” can override semantic analysis

Indemnities: how to recognise them

AXA SA –V- GENWORTH FINANCIAL INTERNATIONAL HOLDINGS, INC [2019] EWHC 3376 (COMM)

Key points highlighted by the court



Indemnities: time limits

TOWERGATE FINANCIAL (GROUP) LTD –V- HOPKINSON & ORS [2020] EWHC 984 (COMM)

- Another indemnity in a SPA relating to mis-selling of financial products
- SPA was dated 5 August 2008; indemnity had a 7-year time limit on claims
- Since then:
 - FCA had started seeking information in mid-2012
 - It flagged “a number of major issues” in early 2013
 - Insurers were notified on 5 March 2013
 - Claimants had identified 72 possible mis-selling claims by June 2013
- Notice of potential claim was dated 29 July 2015




This was before the seventh anniversary of the SPA...but only just

Indemnities: time limits

TOWERGATE FINANCIAL (GROUP) LTD –V- HOPKINSON & ORS [2020] EWHC 984 (COMM)

"The Purchaser shall not make any Claims against the Warrantors...unless notice in writing of the relevant matter or thing...is given to the Warrantors as soon as possible and in any event prior to...on or before the seventh anniversary of the date of this Agreement."



Did this mean:

- (i) notice had to be given "as soon as possible", which had to be before the seventh anniversary; OR
- (ii) notice had to be given before the seventh anniversary?

"Prior to...on or before" was a tautology, but the latter specific provision overrode the former general one

Indemnities: time limits

TOWERGATE FINANCIAL (GROUP) LTD –v- HOPKINSON & ORS [2020] EWHC 984 (COMM)

An issue of construction – so regard must be had to the “recent trilogy of classic cases”

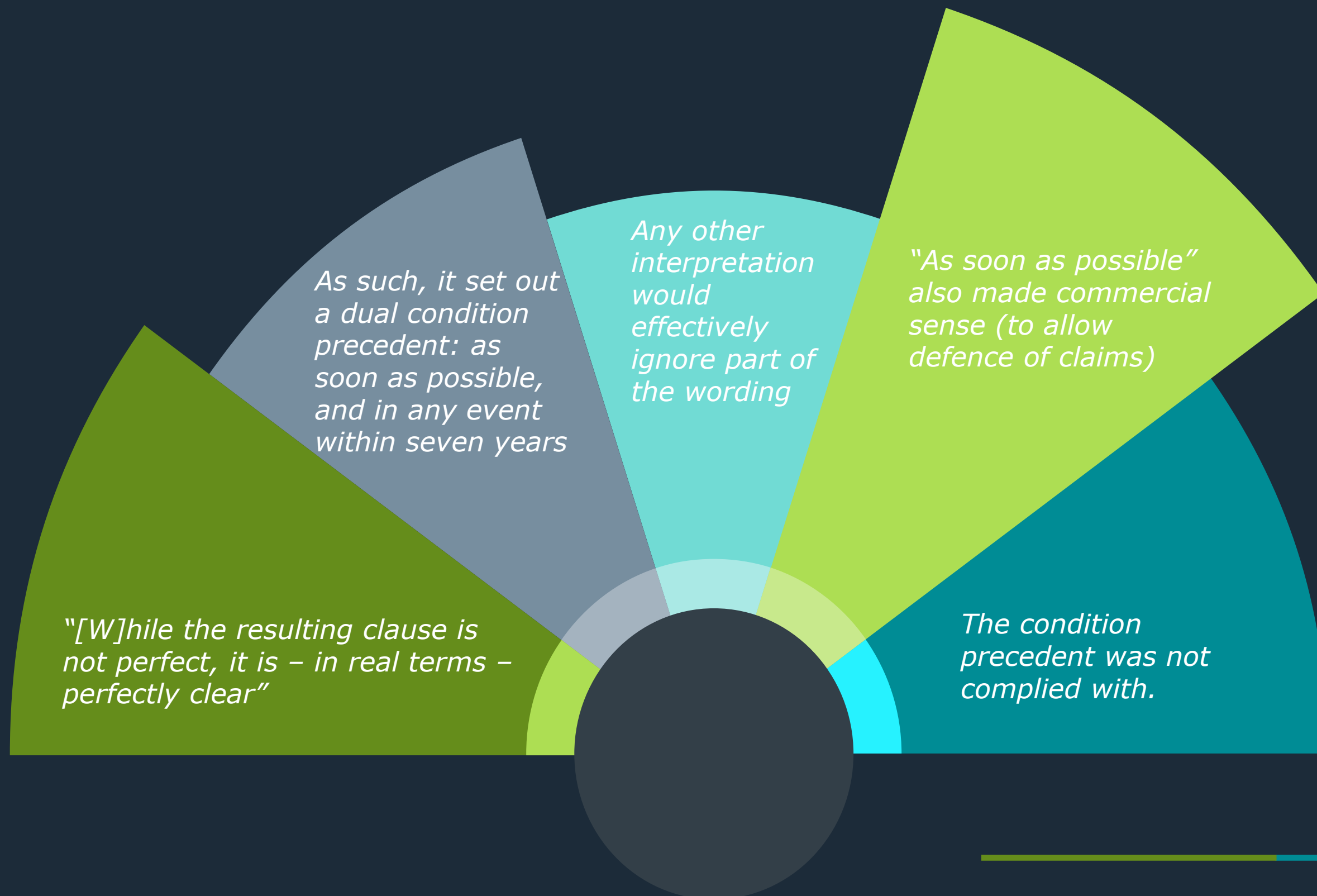
- **Rainy Sky SA –v- Kookmin Bank** [2011] UKSC 50
- **Arnold –v- Britton** [2015] UKSC 36
- **Wood –v- Capita Insurance Services** [2017] UKSC 24

Nobahar-Cookson –v- Hut Group
[2016] EWCA Civ 128

- Time limits are a type of exclusion or limitation clause
- Intention to cut down important legal remedies must be shown by clear words
- No general principle of narrow construction of such clauses – only in cases of ambiguity

Indemnities: time limits

TOWERGATE FINANCIAL (GROUP) LTD –V- HOPKINSON & ORS [2020] EWHC 984 (COMM)



Indemnities

PRACTICE POINTS

- If the clause is intended to be an indemnity, say so
- Don't include contradictory clauses
- Specify matters such as:
 - trigger events;
 - losses covered;
 - methods of calculating payment;
 - any conditions or limitations on recovery
- Remember conditions such as time limits are a form of limitation clause, so draft accordingly
- “As soon as possible” can be valuable, especially if you might want to challenge claims, or take over their conduct
- If you are the indemnified party – read the whole clause. Don't just focus on one point.



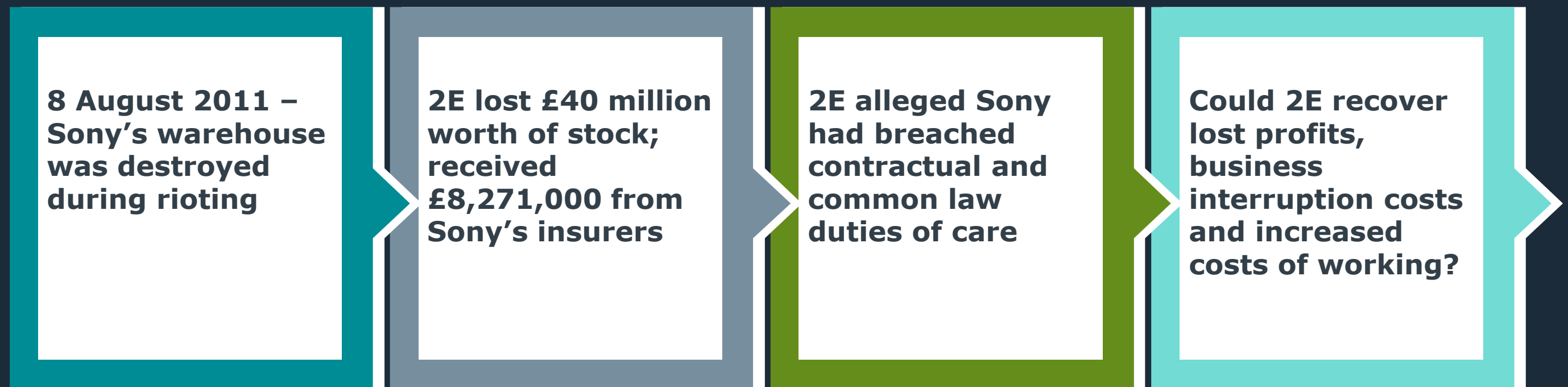
EXCLUSION CLAUSES

Indirect and consequential
loss, and financial caps

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Indirect or consequential loss

2 ENTERTAIN VIDEO LTD & ORS –V- SONY DADC EUROPE LTD [2020] EWHC 972 (TCC)



Indirect or consequential loss

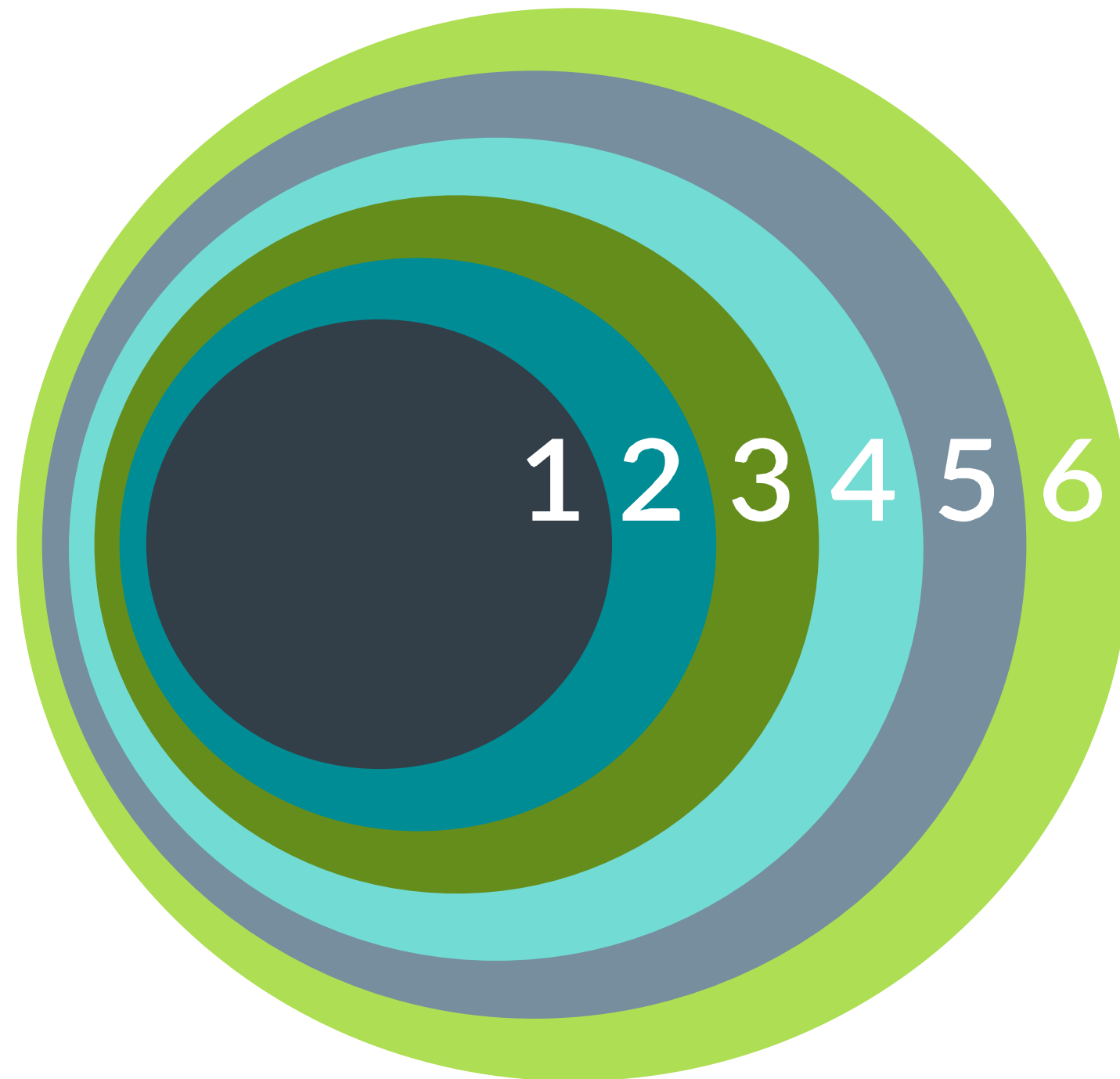
2 ENTERTAIN VIDEO LTD & ORS –V- SONY DADC EUROPE LTD [2020] EWHC 972 (TCC)

- *Neither party shall be liable for its failure or delay in performing any of its obligations hereunder if such failure or delay is caused by circumstances beyond the reasonable control of the party affected including but not limited to...riot....*
- *Neither party shall be liable...for any indirect or consequential loss or damage including (but only to the extent that such are indirect or consequential loss or damage only) but not limited to loss of profits, loss of sales, loss of revenue...loss or waste of management or staff time or interruption of business.*
- *[T]he aggregate liability of [Sony]...for all breaches of...this Agreement or for any losses or liabilities which are the subject of any indemnity by [Sony], whether in contract, tort, for breach of statutory duty or otherwise, shall not in any event exceed the sum of £5,000,000 (five million pounds).*

Indirect or consequential loss

2 ENTERTAIN VIDEO LTD & ORS –V- SONY DADC EUROPE LTD [2020] EWHC 972 (TCC)

IT WAS COMMON GROUND THAT THE RIOTS WERE UNFORESEEN AND UNPRECEDENTED. HOWEVER....



- 1** Previous unauthorised entry
- 2** Warnings given of inadequate security and fire precautions
- 3** Additional security would have probably prevented or delayed the attack
- 4** Installation of sprinklers would have suppressed fire
- 5** Not, therefore, circumstances beyond Sony's reasonable control
- 6** Force majeure defence not available

Indirect or consequential loss

2 ENTERTAIN VIDEO LTD & ORS –V- SONY DADC EUROPE LTD [2020] EWHC 972 (TCC)

- *Neither party shall be liable...for any indirect or consequential loss or damage including (but only to the extent that such are indirect or consequential loss or damage only) but not limited to loss of profits, loss of sales, loss of revenue...loss or waste of management or staff time or interruption of business.*
- Words in brackets were confusing and negated the examples
- **Hadley –v- Baxendale** (1854) 9 Ex 341 therefore applied, with the two limbs:
 - losses naturally arising
 - losses in contemplation of parties as probable result of breach
- *"The loss of profits and business interruption costs...do not constitute indirect or consequential loss or damage within the meaning of [this clause]."*

Caps on liability

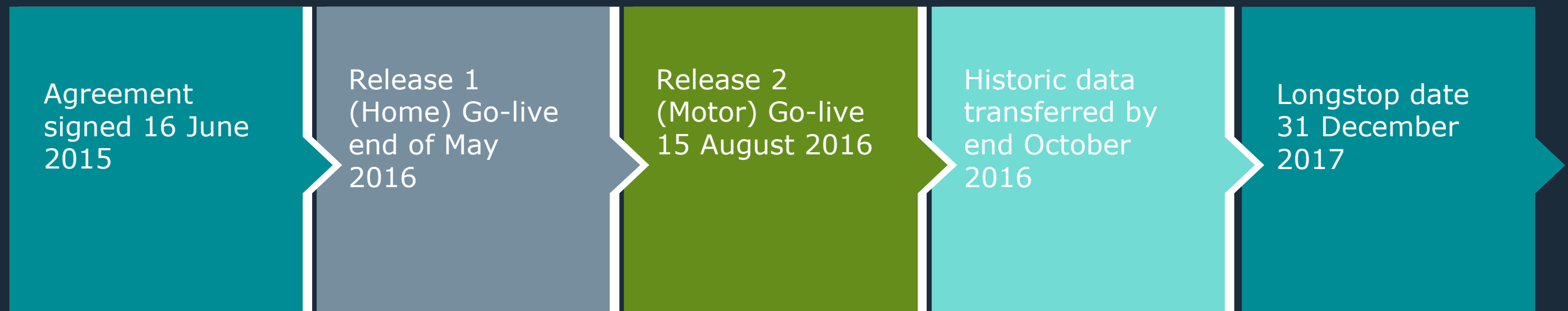
2 ENTERTAIN VIDEO LTD & ORS –V- SONY DADC EUROPE LTD [2020] EWHC 972 (TCC)

- *[T]he aggregate liability of [Sony]...for all breaches of...this Agreement or for any losses or liabilities which are the subject of any indemnity by [Sony], whether in contract, tort, for breach of statutory duty or otherwise, shall not in any event exceed the sum of £5,000,000 (five million pounds).*
- This covered everything – including indemnity obligations
- Had this been reached via the £8.27 million insurance payout?
- Discharge and release agreement stated that the payout settled Sony's liability for loss of the goods...but not for other breaches, or for consequential or business interruption losses
- The contractual cap of £5 million had not been exhausted.

Wasted expenditure

CIS GENERAL INSURANCE LTD –V- IBM UNITED KINGDOM LTD [2021] EWHC 347 (TCC)

Co-op engaged IBM to supply and manage a new IT system for its home and motor insurance business



However: Go-Live dates not met; Co-op refused to pay IBM; IBM purported to terminate; Co-op alleged repudiatory breach.

Wasted expenditure

CIS GENERAL INSURANCE LTD –V- IBM UNITED KINGDOM LTD [2021] EWHC 347 (TCC)

- *"...[N]either party shall be liable...for any Losses arising under and/or in connection with this Agreement (whether in contract, tort (including negligence), breach of statutory duty or otherwise) which are indirect or consequential Losses, or for loss of profit, revenue, savings (including anticipated savings), data..., goodwill, reputation (in all cases whether direct or indirect) even if such Losses were foreseeable and...a party had been advised of the possibility that such Losses were in the contemplation of the other party...."*
- Did this exclude the wasted expenditure claim?

Wasted expenditure

CIS GENERAL INSURANCE LTD –V- IBM UNITED KINGDOM LTD [2021] EWHC 347 (TCC)

- *"The lodestar is that the damages should represent the value of the contractual benefits of which the claimant has been deprived by the breach..."* Lord Scott, ***The Golden Strait Corporation –v- Nippon Yusen Kubishka Kaisa*** [2007] UKHL 12
- This can be measured by:
 - what would be needed by the claimant to achieve the expected contractual benefit ("expectation basis"); or
 - expenditure incurred in reliance on the defendant's promise ("reliance basis")
- Wasted expenditure could, in theory, be recovered, but was it covered by the wording in the exclusion clause?

Wasted expenditure

CIS GENERAL INSURANCE LTD –V- IBM UNITED KINGDOM LTD [2021] EWHC 347 (TCC)



“Wasted expenditure” is merely a different method of quantifying the loss – *“it does not change the characteristics of the losses for which compensation is sought.”*

Co-op’s claim was therefore excluded.

Indirect and consequential losses

PRACTICE POINTS

- Watch your wording – these clauses are not “boilerplate”
- Draft clearly – say what you mean, don’t try for cute or sneaky
- Consider the likely losses – and draft for them
 - Bring heads of loss under the second Hadley v Baxendale limb by bringing to the attention of the counterparty



BREACH OF CONTRACT

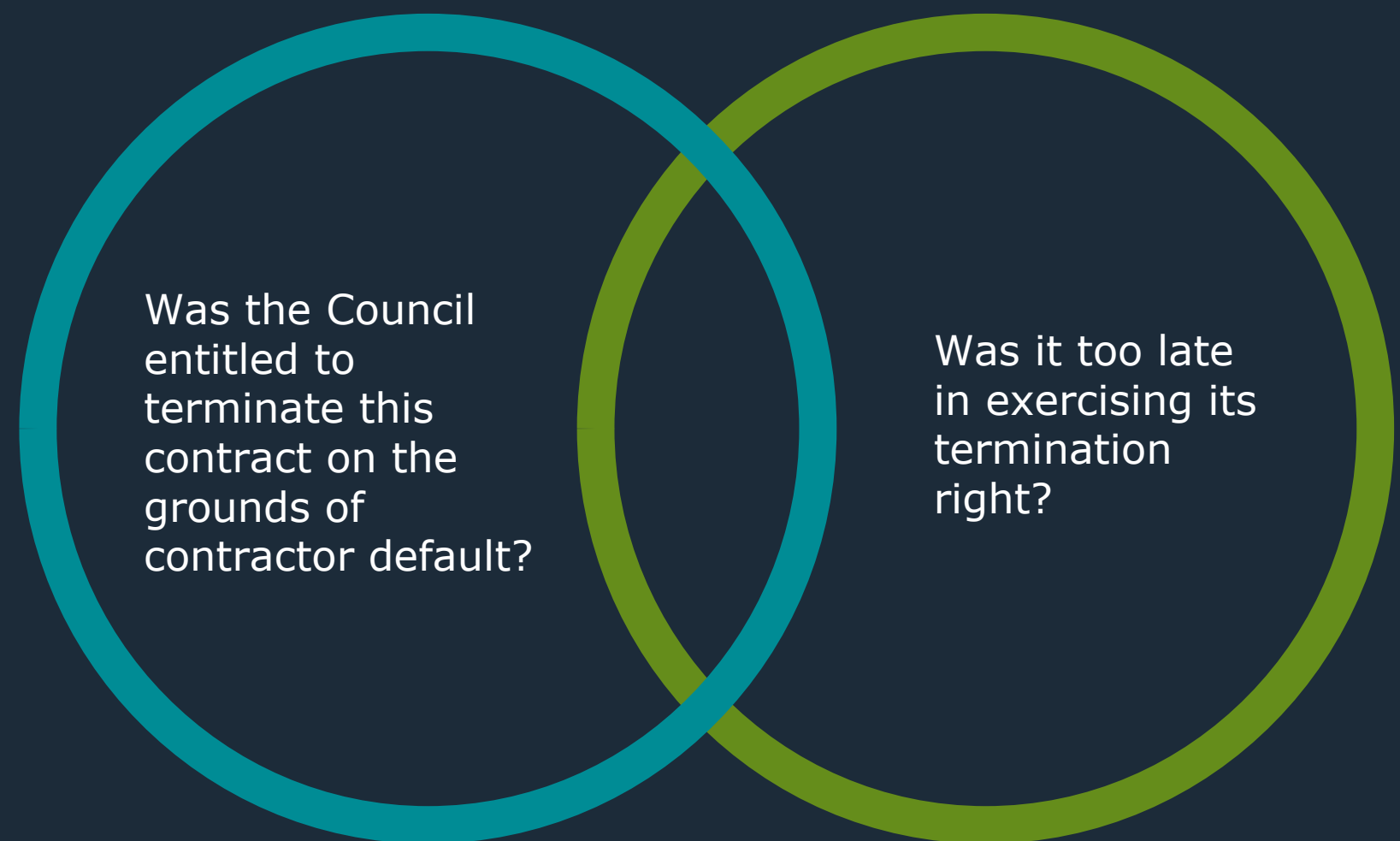
Terminating for Breach

3

Breach of contract: terminating for breach

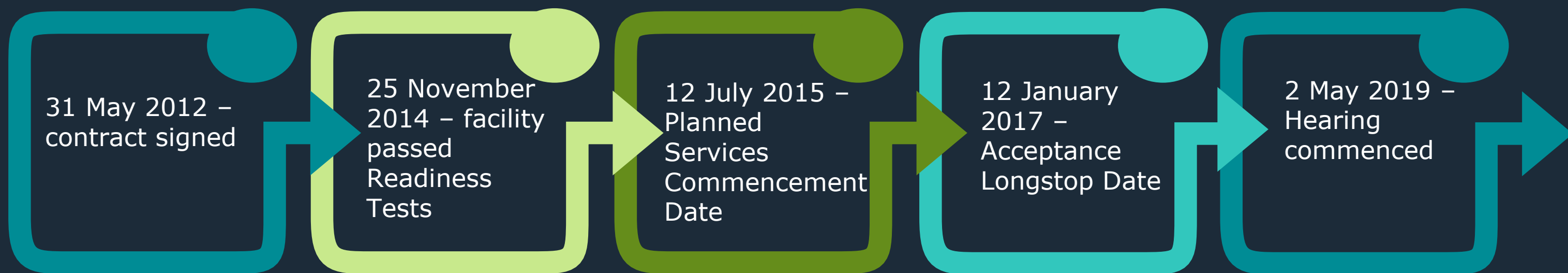
ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)

25-year contract for design, construction, commissioning, operation and maintenance of a waste treatment facility, which never operated well enough to pass the Acceptance Tests



Breach of contract: terminating for breach

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)

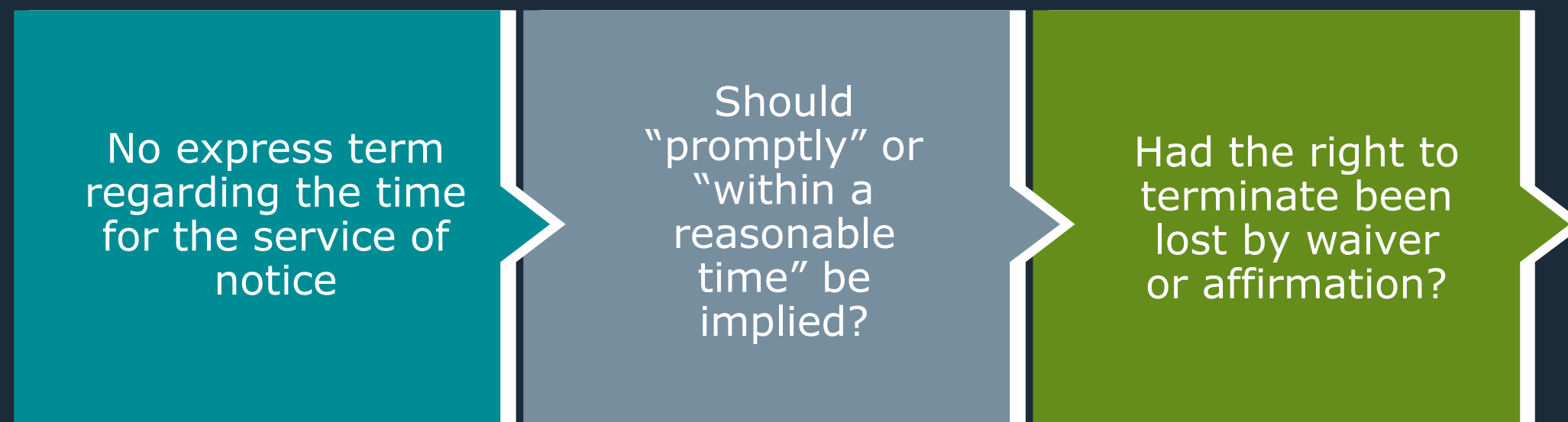


NB: Acceptance tests still not passed

Breach of contract: terminating for breach

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)

Given the timeline, was the Council still entitled to serve notice of termination?



Breach of contract: terminating for breach

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC): IMPLIED TERM?

- Pepperall J: *"I reject...the argument that there is an immutable rule of law that all rights of termination must be exercised within a reasonable time after such right first arises."*
- In charterparty cases, business efficacy and fairness as between parties call for promptness to be implied
- This, however, was a 25-year contract:
 - giving the contractor time might allow it to salvage the project;
 - "stalemate" if the facility fails acceptance testing, but deadline is missed - leaving parties with a barely functioning facility and payment at reduced rates
- Implying the term here would not be commercial, practical, or obvious
- Waiver by election/affirmation was the better question to consider.

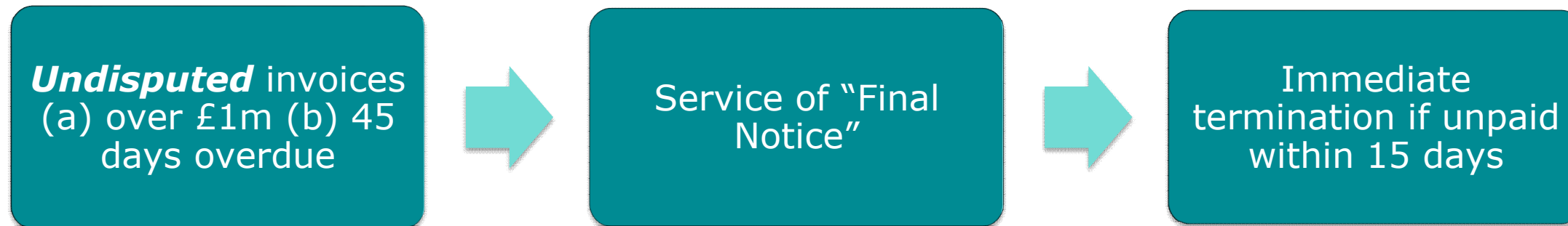
Breach of contract: terminating for breach

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC): AFFIRMATION/WAIVER?

- **The Kanchenjunga** [1990] 1 Lloyd's Rep 391 (Lord Goff):
 - The right must be exercised (by words or conduct, but must be unequivocal)
 - Court must make a finding one way or the other
 - A question of fact in each case
- Council's right to terminate arose on 12 January 2017:
 - This was 2.5 years before close of evidence
 - Council had continued to perform
 - However, facility had still not passed Acceptance Tests
- Council had not affirmed contract or waived its right to terminate

Breach of contract: terminating for breach

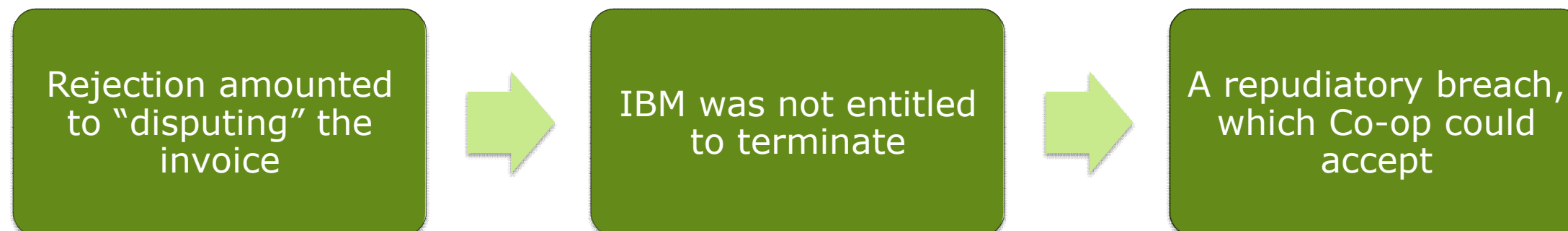
CIS GENERAL INSURANCE LTD –V- IBM UNITED KINGDOM LTD [2021] EWHC 347 (TCC)



24 March 2017: Invoice received by Co-op and rejected owing to lack of accompanying Purchase Order

22 June 2017: IBM served Final Notice

27 July 2017: IBM served notice of termination

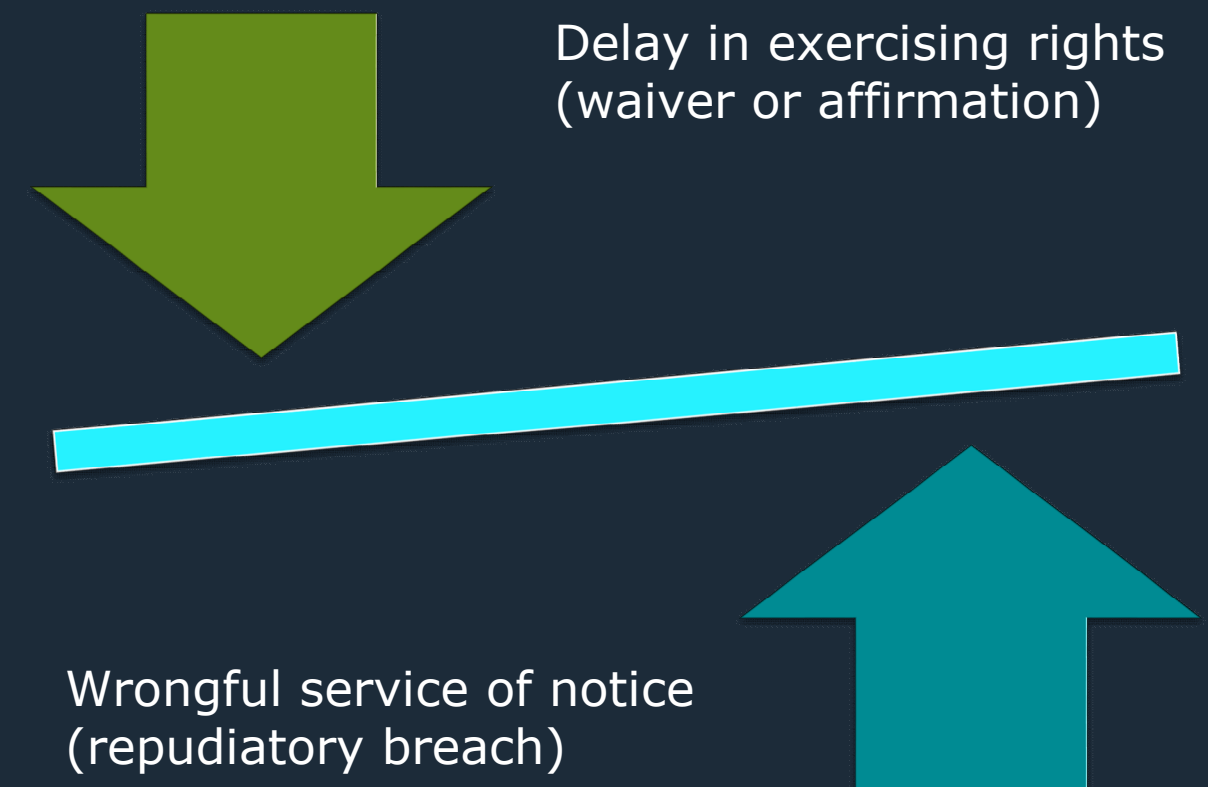


Termination for breach

PRACTICE POINTS

Getting it right often involves treading a fine line

Wording of the contract – including any procedural steps – is key





GOOD FAITH

4

Good faith

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)

25-year contract for the design, construction, financing, commissioning, operation and maintenance of a mechanical biological waste treatment plant

Should it be implied that contractual discretion would be exercised in good faith?

- No, where the contractual right is absolute
- No, in the case of a termination rights (**Lomas –v- JB Firth Rixon Inc** [2012] EWCA Civ 419)

Should a term be implied of good faith and co-operation generally?

- For certain categories of contract, yes
- Typically “relational” contracts (**Yam Seng –v- International Trade Corp** [2013] EWHC 111 (QB) – followed in **Bates –v- Post Office** [2019] EWHC 606 (QB)

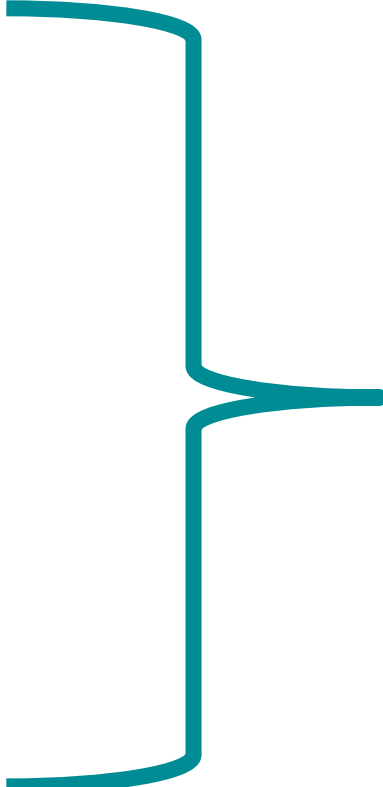
Was implication of such a term precluded?

- A “sole remedy” clause does not affect the implication of terms
- Neither does an entire agreement clause (Chitty on Contracts, 33rd. Ed. at para 37-073).

Good faith: relational contracts

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)

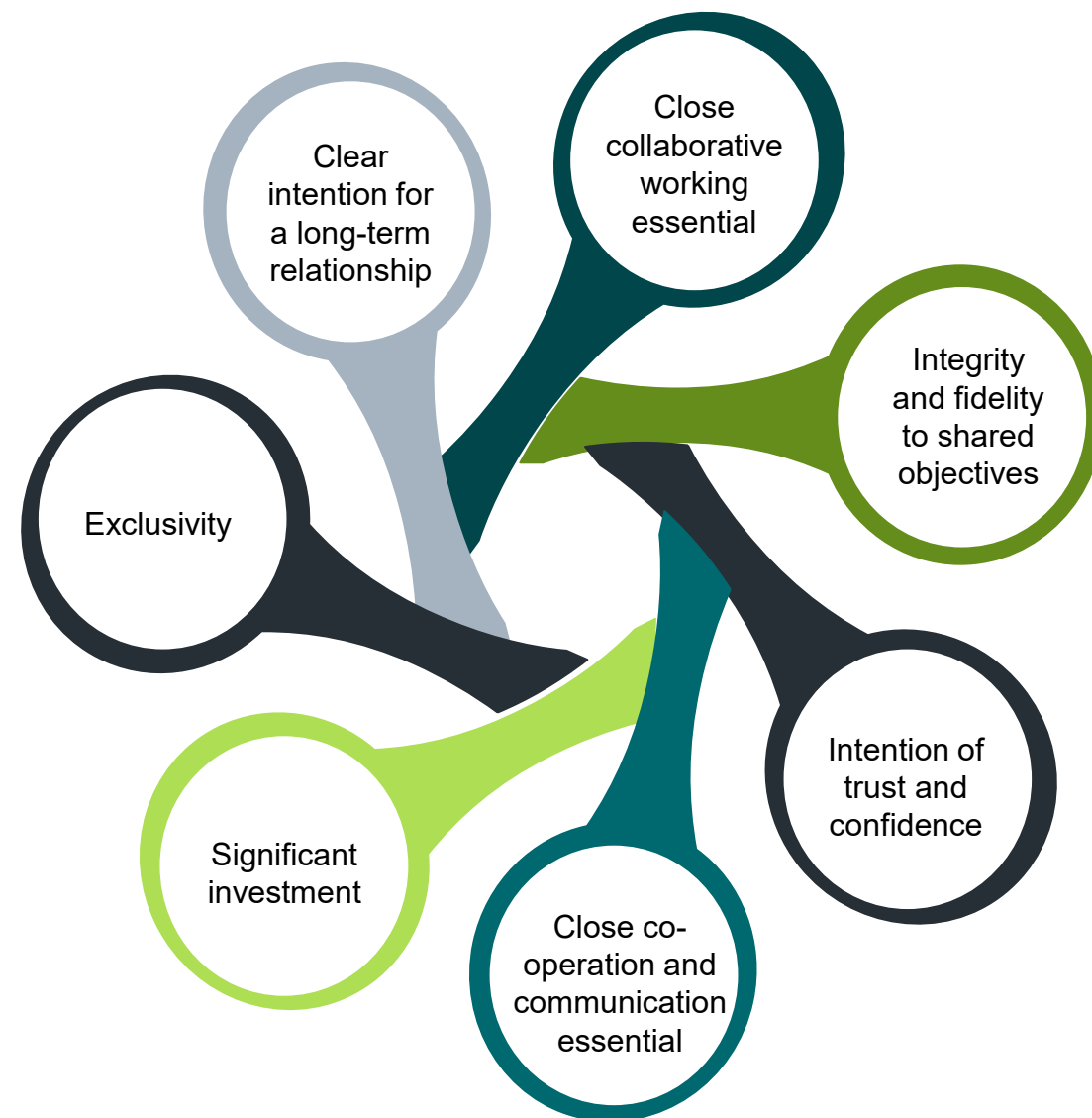
- No express terms preventing implication
- Mutual intention for a long-term relationship
- Intention to act with integrity and fidelity
- Commitment to collaboration
- Spirits and objective may not be easily captured in writing
- Trust and confidence (distinguish fiduciary relationships)
- High degree of communication, co-operation and predictable performance, based on expectations of loyalty
- Substantial financial commitment
- (Possibly) exclusivity



*Fraser J's "non-exhaustive" list:
Bates -v- Post
Office, supra,
paras 725-726*

Good faith: relational contracts

ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)



"I conclude that this 25-year PFI contract is a paradigm example of a relational contract in which the law implies a duty of good faith."

However, the Council's insistence that the facility passed Acceptance Tests was in no way inconsistent with this.



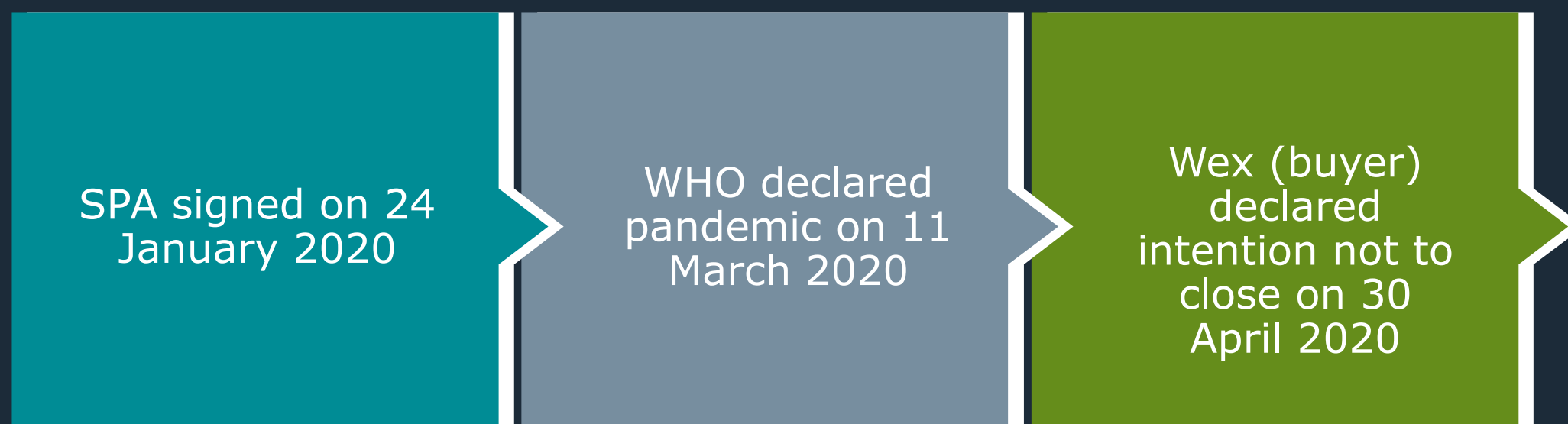
COVID-19

MAC/MAE and change of
law clauses

5

Covid-19: material adverse change/effect clauses

TRAVELPORT & ORS LTD –V- WEX INC [2020] EWHC 2670 (COMM)



Covid-19: material adverse change/effect clauses

TRAVELPORT & ORS LTD –V- WEX INC [2020] EWHC 2670 (COMM)

- Did a Material Adverse Effect (“MAE”) clause in the SPA entitle the Buyer (Wex) to make this decision?
- Condition precedent: *“Since the date of this Agreement there shall not have been any Material Adverse Effect and no event, change, development, state of facts or effect shall have occurred that would reasonably be expected to have a Material Adverse Effect.”*

“Material Adverse Effect”: anything which has significant effect on the business or would prevent or materially delay the purchase

Except for changes in law/regulatory change
(Exception 1)

Except for impact of the pandemic, **unless** disproportionate impact on the Target Companies in the context of the industries in which they operate
(Exception 2)

Covid-19: MAC/MAE clauses - interpretation

TRAVELPORT & ORS LTD –V- WEX INC [2020] EWHC 2670 (COMM)

How did Exclusion 2 apply?

- Common ground that if the “disproportionate impact compared to industries” qualifier did not kick in, Wex would fail

How to define “industries” in order to make a comparison?

- “Industry” is broader than “market” or “sector”
- Use of plural – significant in a formal document
- B2B payments industry, not travel payments alone

Covid-19: MAC/MAE clauses as a risk allocation mechanism

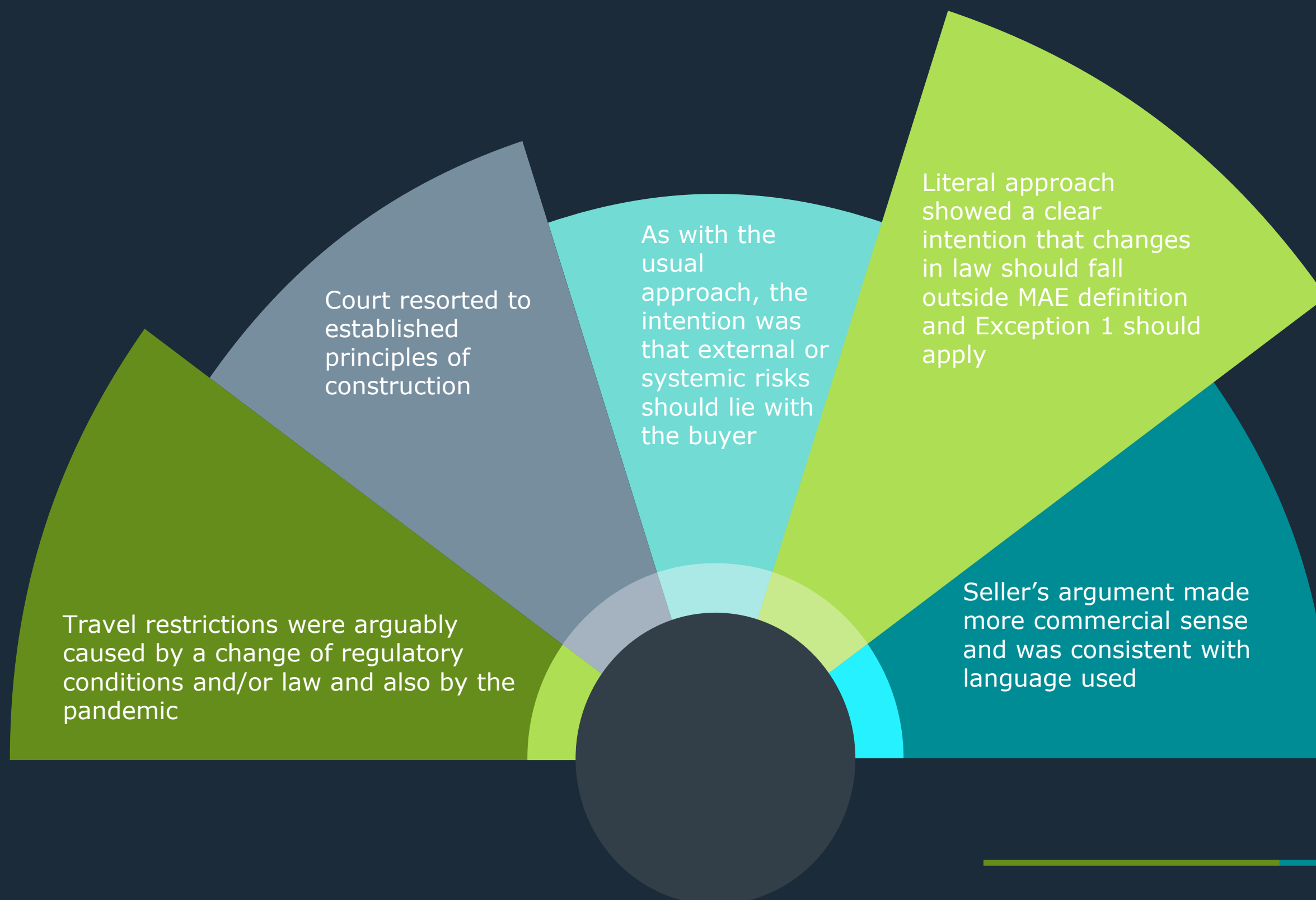
TRAVELPORT & ORS LTD –V- WEX INC [2020] EWHC 2670 (COMM)

- Starting point – risk of a MAC is on the seller
- Systemic or industry risks are carved out, i.e., allocated to the buyer, as are known risks (purpose of due diligence)
- Target-specific risks, over which seller has/had control, are returned to the seller



Covid-19: MAC/MAE clauses

TRAVELPORT & ORS LTD –V- WEX INC [2020] EWHC 2670 (COMM)



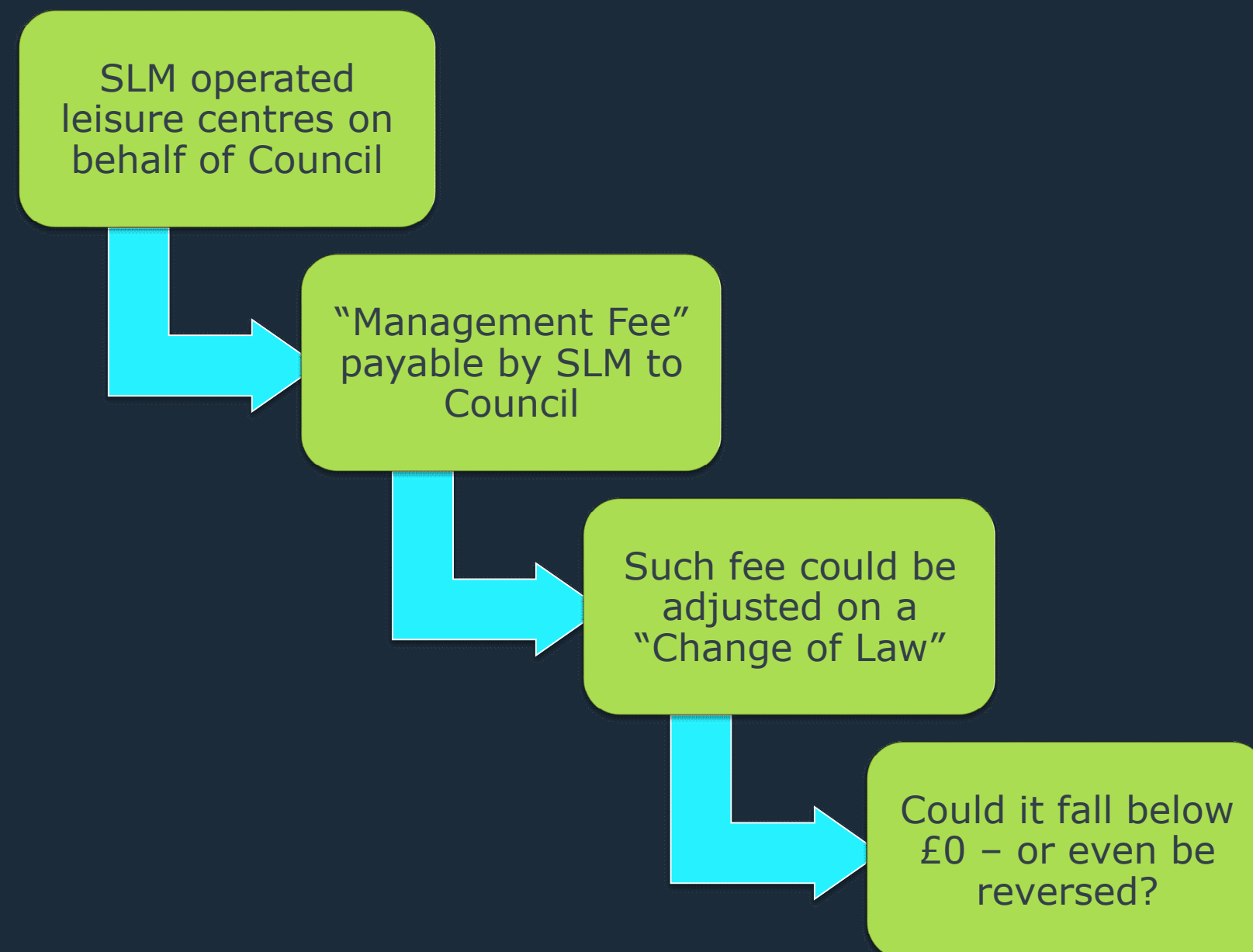
Covid-19: MAC/MAE clauses: practice points

TRAVELPORT & ORS LTD –V- WEX INC [2020] EWHC 2670 (COMM)

- Exact wording was carefully scrutinised:
 - draft clearly
 - use language consistently
- Court will be reluctant to imply additional terms, especially where a clause is heavily negotiated (as here)
- Ensure the clause is workable:
 - take care over comparators (“industry” rather than “market”)
 - is wording overly convoluted?
- Appeal is likely

Covid-19: change in law clauses

WESTMINSTER CITY COUNCIL –V- SPORTS AND LEISURE MANAGEMENT LTD [2021] EWHC 98 (TCC)



Key contextual points:

- A standard form document drafted by experienced lawyers
- Essentially a concession agreement (typically, contractor bears a significant degree of risk)
- Usual approach is that general changes in law fall on contractor (ordinary course of business)

Covid-19: change in law clauses

WESTMINSTER CITY COUNCIL –V- SPORTS AND LEISURE MANAGEMENT LTD [2021] EWHC 98 (TCC)

Textual factors prevailed – and only pointed to one conclusion

Definition of Management Fee

“the net fee payable by the Contractor to the Authority...”

Clause 26.1

Basic obligation: “The Contractor shall pay the Authority the Management Fee...”

Clause 26.2-26.8

“One way” process for calculation and payment

Covid-19

GENERAL PRINCIPLES

Covid itself may well not raise any specific legal issues

Cases will invariably turn on interpretation/construction questions

In both cases thus far, wording was critical – but the normal rules of construction applied.



“WILFUL”

6

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“Wilful”

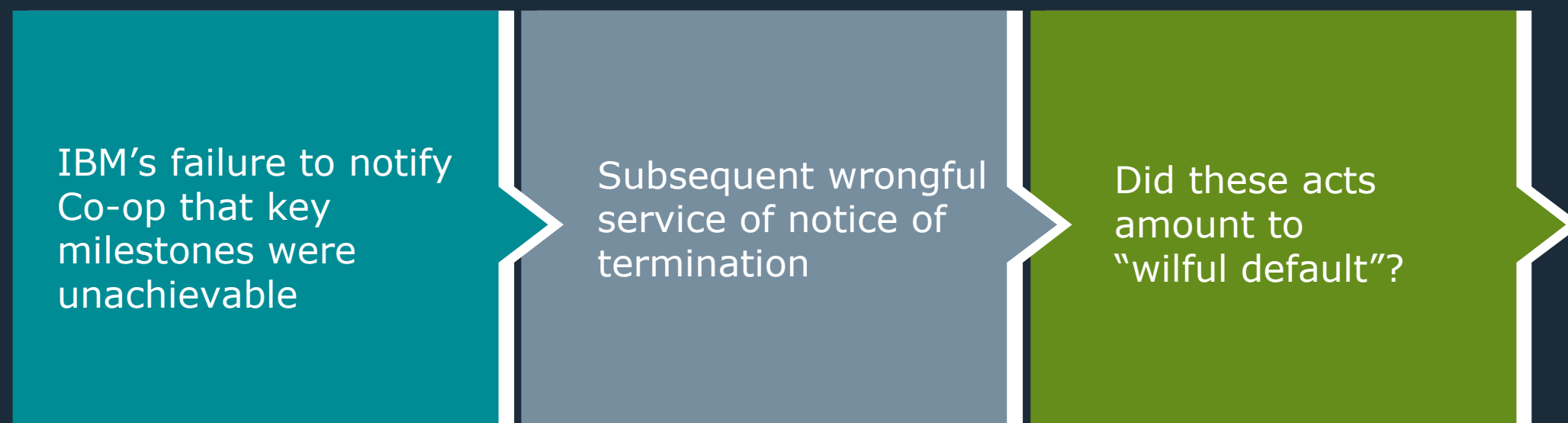
ESSEX COUNTY COUNCIL –V- UBB WASTE (ESSEX) LTD [2020] EWHC 1581 (TCC)

- Contract included a requirement for waste to be delivered to the Facility. Wilfully directing waste, or wilfully allowing it to be delivered, elsewhere was a “Compensation Event”
- Asbestos scare led to a two-step process:
 - waste diverted to a waste transfer station; then
 - delivered to the Facility
- Was this a Compensation Event?
- “Wilful” signified “*intentional or deliberate*” conduct
- Council had not wilfully directed the diversion of waste
- However, it did nothing to press its contractors to make deliveries

“...I do not criticise the Authority for taking a risk-averse approach...but in doing so it wilfully allowed the deliveries of waste to be diverted away from the facility.”

“Wilful”

CIS GENERAL INSURANCE LTD –V- IBM UNITED KINGDOM LTD [2021] EWHC 347 (TCC)



“Wilful default” defined as *“an intentional breach of the Agreement with either an intent to cause harm or recklessness with regard to the consequences of the breach.”*

No intentional breach: each party had believed it was entitled to act as it did.

Conclusion

KEY THEMES

- Good faith and the continued rise of relational contracts
- Otherwise: focus has remained on construction of contractual wording
 - Procedural matters
 - Indemnities and exemption clauses
 - Covid-related issues – new circumstances, same law
- The “classic” construction cases still very much front and centre:
 - **Investors Compensation Scheme –v- West Bromwich Building Society** [1997] UKHL 28
 - **Rainy Sky SA –v- Kookmin Bank** [2011] UKSC 50
 - **Arnold –v- Britton** [2015] UKSC 36
 - **Wood –v- Capita Insurance Services Ltd** [2017] UKSC 24

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