Breakfast Briefing: Contract Law Update

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Introduction

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(2) Principles of Contractual Interpretation - *Arnold -v- Britton & Others [2015] UKSC 36*

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1. Penalty Clauses

Cavendish Square Holdings BV -v- Makdessi; ParkingEye Ltd -v- Beavis [2015] UKSC 67

The Facts

(1) *Cavendish*:

M was a majority shareholder in a large advertising and marketing group based in the Middle East. He entered into an agreement with C for the purchase of the majority of that shareholding – though not all of it. The purchase price contained a goodwill element to it which stemmed from restrictive covenants put in place which would prohibit M from competing with the company following the sale – these were intended to preserve the purchase price paid by C for the shareholding and the valuation of the company generally. The purchase monies were to be paid in a series of instalments.

There were 2 clauses which were in issue. Clause 5.1 provided that if the restrictive covenants were breached by M, C would not have to pay the final two instalments towards the purchase price. Clause 5.6 stated that, further to clause 5.1, if the restrictive covenants were breached, C would obtain a right to purchase M's remaining shareholding in the company which had not formed part of the sale, the price would be calculated without reference to the original purchase price of the shares and would exclude the value of M's goodwill in the sale.

M breached the restrictive covenants and C consequently exercised their rights under the contract. M argued they were invalid penalty clauses. At all times the parties were legally advised and were both of equal bargaining power.

(2) ParkingEye:

P was the contracted operating agent of a car park at a retail park. The car park was owned by British Airways Pension Fund on whose behalf P was acting. There were signs displayed within the car park which allowed for users to park vehicles free of charge for 2 hours. Any overstaying beyond that time was subject to a charge of £85. B used the car park and overstayed. He was charged £85 for so doing by P. B refused to pay and argued that the charge amounted to a breach of the Unfair Terms in Consumer Contract Regulations 1999 and/or was a penalty clause.

The Decision

The Supreme Court reviewed the case law on penalty clauses. They held that the policy behind the unenforceability of penalty clauses remained sound. However, they emphasised that there was a need to outline the Court's jurisdiction in dealing with such clauses and move away from application of Lord Dunedin's principles

in *Dunlop Pneumatic Tyre Co Ltd -v- New Garage and Motor Co Ltd [1915] AC 79* in the rigid and steadfast way that had evolved since that judgment.

The 2 Stage test:

At paragraph 11 the Court said:

> *"The penalty rule as it has been developed by the judges gives rise to two questions, both of which have a considerable bearing on the questions which arise on these appeals. In what circumstances is the rule engaged at all? And what makes a contractual provision penal?"*

(a) Jurisdiction according to classification

The Court drew a distinction between clauses which were properly classified as primary obligations and those which were classified as secondary obligations. Jurisdiction to review a clause did not apply to the performance of primary obligations – to do so would be to assess the fairness of the contract which was not the Court's role. As such, it is only clauses which amount to a secondary obligation which would give a Court jurisdiction to review them.

As to what was a secondary obligation, this principally included (in the context of penalty clauses) obligations which provided for a remedy ancillary to the performance of a primary obligation – though it need not be a remedy limited to monetary payments – other remedies such as assignment of a right could be provided, for example [16].

(b) Assessment of whether or not a clause is penal

Concern was expressed by the Court that Lord Dunedin's 4 principles in *Dunlop* has now been given a quasi-codified status such that they provided firm categories of clauses by which all clauses should be compared to. At paragraph 22:

> *"Lord Dunedin's speech in Dunlop achieved the status of a quasi-statutory code in the subsequent case-law. Some of the many decisions on the validity of damages clauses are little more than a detailed exegesis or application of his four tests with a view to discovering whether the clause in issue can be brought within one or more of them. In our view, this is unfortunate. In the first place, Lord Dunedin proposed his four tests not as rules but only as considerations which might prove helpful or even conclusive "if applicable to the case under consideration". He did not suggest that they were applicable to every case in which the law of penalties was engaged. Second, as Lord Dunedin himself acknowledged, the essential question was whether the clause impugned was "unconscionable" or "extravagant". The four tests are a useful tool for deciding whether these expressions can properly be applied to simple damages clauses in standard contracts. But they are not easily applied to more complex*

> *cases. To deal with those, it is necessary to consider the rationale of the penalty rule at a more fundamental level. What is it that makes a provision for the consequences of breach "unconscionable"? And by comparison with what is a penalty clause said to be "extravagant"? Third, none of the other three Law Lords expressly agreed with Lord Dunedin's reasoning, and the four tests do not all feature in any of their speeches."*

There was thus endorsement of a more broader primary question:

> *"The question was: what was the nature and extent of the innocent party's interest in the performance of the relevant obligation?" [23]*

That led to the conclusion at paragraph 32 where there was the enunciation of a secondary question once the primary question above is answered – this is the proportionality limb:

> *"The true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation. The innocent party can have no proper interest in simply punishing the defaulter. His interest is in performance or in some appropriate alternative to performance. In the case of a straightforward damages clause, that interest will rarely extend beyond compensation for the breach, and we therefore expect that Lord Dunedin's four tests would usually be perfectly adequate to determine its validity. But compensation is not necessarily the only legitimate interest that the innocent party may have in the performance of the defaulter's primary obligations. This was recognised in the early days of the penalty rule, when it was still the creature of equity, and is reflected in Lord Macclesfield's observation in Peachy (quoted in para 5 above) about the application of the penalty rule to provisions which were "never intended by way of compensation", for which equity would not relieve. It was reflected in the result in Dunlop. And it is recognised in the more recent decisions about commercial justification. And, as Lord Hodge shows, it is the principle underlying the Scottish Authorities."*

That meant that interests such as deterrence must also be factored in. In addition, interests which affected one party outside the scope of the contract in question also fall to be considered – such as the interests of an agent performing an obligation to his principal which would be fulfilled by the agents contract with the end customer, for example, would presumably also now be capable of forming part of the assessment – provided of course there was sufficient linkage between the interest and the contractual clause in place.

Once those interests were identified, the second aspect of the proportionality of the remedy specified to those interests falls to be assessed. It seems fairly trite that the more important the interest behind the clause, the more latitude will be given in the assessment of proportionality to the quantum or extent of the remedy. In this analysis the previous categorisations of the remedy being 'exorbitant', 'unconscionable' etc. are still of relevance.

However, the Supreme Court also established a presumption. In circumstances where the parties were of equal bargaining power and properly advised throughout the negotiations of the clause in question, there is a presumption that the interests encapsulated within the eventual drafting of the clause are legitimate and the remedies therein provided, proportional to those interests. One can only surmise that that would be a very difficult presumption to rebut the more the history of dealing between the parties evident and especially where similar clauses have appeared in previous dealings between the parties:

> *"But for all that, the circumstances in which the contract was made are not entirely irrelevant. In a negotiated contract between properly advised parties of comparable bargaining power, the strong initial presumption must be that the parties themselves are the best judges of what is legitimate in a provision dealing with the consequences of breach. In that connection, it is worth noting that in Philips Hong Kong at pp 57-59, Lord Woolf specifically referred to the possibility of taking into account the fact that "one of the parties to the contract is able to dominate the other as to the choice of the terms of a contract" when deciding whether a damages clause was a penalty." [35]*

Application to the Cases

(1) Cavendish

- Clause 5.1 was treated with an 'open mind' by their Lordships as to its classification as a primary obligation as opposed to a secondary obligation. For what it is worth, the author's view is that it was plainly a primary obligation since it involved the purchase price being paid. In respect of that clause the interest which C had in it was to deter M from breaching the restrictive covenants and thus undermining the value of the shares which C had purchased. That was, in any event, a legitimate interest which was proportionately provided for in the clause itself.

- Clause 5.3 was a secondary obligation which was contingent on the primary obligations being performed – it was therefore reviewable. The interests C had in this clause were the same as in relation to clause 5.1 and again the clause provided for a proportional remedy to those aims.

- *Cavendish* was a case to which the presumption applied.

- For those reasons the clauses were enforceable and upheld.

(2) ParkingEye

- The challenge under the 1999 Regulations failed. There was a 'significant imbalance' in the parties respective rights as a consequence of the clause. However, that imbalance was not 'contrary to good

faith' and therefore not unfair. In short a reasonable motorist would have likely agreed to the clause had it been specifically negotiated.

- Though P expressly conceded that the charge was not a genuine pre-estimate of loss, that did not mean it was a penalty clause.

- It was a secondary obligation which could be reviewed. It came about as a result of the primary obligations not being complied with.

- There was a legitimate interest in the charge – it included the interests of the owner of the car park, the retail outlets, and other customers. There was also a deterrent element.

- A charge of £85 was not out of all proportion with those interests.

- The clause was therefore upheld as enforceable.

Conclusion

Though the law remains, to intent and purposes, the same as before in terms of the policy and rationale for the penalty rule, the way that it is analysed by the Court has now changed. The procedure is now broken down as follows:

(1) Is the obligation in question a secondary obligation?

(2) If yes, is the clause penal by reference to:

a. The aims behind the clause by the party benefiting from it; and

b. Whether the remedy provided for is proportional to those aims.

The presumption that the answers to (2)(a) and (b) will be 'yes' in cases where the parties are of equal bargaining power and have had the benefit of advice throughout, is rebuttable, but nonetheless strong.

2. Principles of Contractual Interpretation

Arnold -v- Britton & Others [2015] UKSC 36

The Facts

Arnold concerned a holiday park in South Wales. The park contained a number of chalets who were each the subject of 99 year leases. The leases contained covenants for both the tenant and the landlord. Further to this the leases also provided for a service charge to be paid to the landlord for the general upkeep and maintenance of the park itself. The service charge was expressed to in clause 2(3) of 70 of the leases as follows:

> *"To pay the Lessor without any deduction in addition to the said rent a proportionate part of the expenses and outgoings incurred by the Lessor in the repair maintenance renewal and the provision of services hereinafter set out the yearly sum of Ninety Pounds and value added tax (if any) for the first three years of the term hereby granted increasing thereafter by Ten Pounds per Hundred for every subsequent three year period or part thereof."*

In essence, the appellants (the tenants under the leases) argued that the service charge clause did not read such as to provide for a compound 10% uplift every three years on the base charge of £90 but that it provided that they would pay the landlord their reasonable expenses incurred in maintaining the site 'up to' a maximum of £90 plus the uplift. They argued this on the apparent existence of a contradiction within the term in question - the first half of it providing for a 'proportionate' service charge to the landlords maintenance costs, and the second half providing for an amount by way of a calculation which could yield a disproportionate level of charge. Accordingly, due to this contradiction they asked the Court to give more weight to the first half of the clause and make the second half's calculation subject to a capping provision to an amount 'proportionate' to the landlords incurred maintenance costs.

The landlord contended that the clause should be construed as read so as to provide for an uplift and if this amount exceeded the landlord's maintenance costs for the year then that was still the amount which should be paid. Equally, the landlord contended that the calculation could provide for an amount below their maintenance costs with them bearing the costs over and above that level. In either event, the landlord submitted that an ordinary reading of the clause could not be interpreted as capping the level of charge.

The Decision

The Majority

At paragraph 14 Lord Neuberger refered to the established factors in *Prenn -v- Simmonds [1971] 1 WLR 1381* and states, at paragraph 15:

"That meaning has to be assessed in light of the (i) the natural and ordinary meaning of the clause and the lease, (ii) any other relevant provisions of the lease, (iii) the overall purpose of the clause and the lease, (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions."

The more developed part of the judgment comes from paragraphs 17-23. In these sections, Lord Neuberger makes it clear that the factors identified above are both hierarchical and qualified thus:

I. 'Ordinary meaning' - the most fundamental principle is to ascertain what the parties agreed from the ordinary meaning of the words in the relevant provision. The Court should always have this as its starting point and, save in unusual instances, departure from them should not be undertaken. The Court is not re-writing the contract but is giving effect to the agreement the parties reached. Even in cases where it is necessary for the Court to look at other factors, the ordinary meaning of the provision lingers, akin to an overriding objective, throughout the interpretation process to ensure that effect is given, so far as is possible, to the parties agreement.

II. 'Other provisions' - Where there is another contractual provision which appears to be at odds with the provision now under scrutiny, the resolution between the two can be dealt with by reference to the other factors but focus should again be on the ordinary meaning of the two conflicting provisions as a first point of recourse. Where there is another provision which supplements or elaborates upon another provision then that other provisions' wording should be the Court's primary assessment. Where ambiguity prevails, then other factors should be examined to ensure correct interpretation of it.

III. 'Knowledge of the parties' - When assessing the facts known to the parties the Court must focus on their knowledge at the time of agreement - it is a snapshot in time of their knowledge at that point which the Court is concerned with - hindsight should be disregarded in this assessment. This factor can, it seems, play a part in the assessment of the everyday meaning of the wording of the provision in question, but also feeds into the assessment of commercial common sense where that factor is engaged. Note that emphasis is applied by Lord Neuberger at paragraph 21 so that the focus is on what was common knowledge to both parties - the contract, by its nature, is bilateral and therefore facts which were known to one party but not to another will not be of assistance in identifying what was actually agreed.

IV. 'Commercial common sense' - This is a factor which is "very important" but which is significantly qualified and is not to be applied without appreciation of its boundaries. In particular:

a) *"Commercial common sense and surrounding circumstances should not be invoked to undervalue the importance of the language of the provision which is to be construed."* [para17] - to that end it must follow that it will not always be necessary to revert to this factor in every case. In short, where the wording is clear and can be interpreted by itself, there will be no need for the Court to look at the other factors;

b) *"Commercial common sense is only relevant to the extent of how matters would or could have been perceived by the parties, or by reasonable people in the position of the parties, as at the date that the contract was made."* [para 18] - The message here being that though what is commercially sensible at the time of the contract may not be commercially sensible at the time of performance. This should not relieve the non-performing party from the bargain they entered into just because it now appears to have been a bad one.

V. In cases where there is an unintended or unforeseen event which occurs, firstly the Court must satisfy itself that the event in question was outside of the scope of the agreement having regard to the language of the contractual provisions, and secondly the Court will always try and interpret the contractual provision now in doubt in accordance from the general intentions of the parties as evidence from the wording of the contract itself. Again the message is clear - the Court must not enter into the territory of re-writing the contract but is giving effect to the agreement insofar as it is able.

Applying this hierarchy to ***Arnold***, Lord Neuberger noted that the effect of the wording of clause 3(2) was that the tenants would be paying over and above the actual maintenance costs of the landlord in him performing his covenants under the lease. Commercially speaking this represented a poor bargain for the tenants since they were adding to the landlords overall profits as opposed to capping them at a level of incurred expenditure – indeed, by 2072 the annual service charge would be £550,000 due to its compound nature. Notwithstanding this, commercial common sense was not a factor which came into the interpretation assessment since the wording of the clause clearly provided for this outcome. He held at paragraph 28:

> *"It is true that the first part of the clause refers to a lessee paying a 'proportionate part' of the cost of the services, and that, unless inflation increases significantly in the next 50 years it looks likely that the service charge payable under each of the 25 leases may exceed cost of providing services to the whole of the Leisure Park. However, if, as I believe is clear, the purpose of the second part of the clause is to quantify the sum payable by way of service charge, then the fact that, in the future, its quantum may substantially exceed the parties' expectations at the time of the grant of the lease is not a reason for giving the clause a different meaning."*

Lord Neuberger therefore interpreted the clause in the landlord's favour, holding that the first half of the clause imposed a liability on the tenants and the second part provides a method for calculating its amount. The clause

went no further than this and did not provide for a cap to be placed on the amount relative to the landlords incurred maintenance costs - whether or not the outcome was commercially prudent for the tenant was irrelevant.

The Minority

For Lord Carnwath however, the matter was not so straightforward and he advocated that an assessment of the clauses' commercial outcome should be undertaken almost immediately in the interpretation process. In his minority speech he referred to a number of authorities which touched upon cases where the language of a clause had yielded unreasonable results (see paragraphs 109-110). Lord Carnwath's approach, therefore, was not to deploy a hierarchy amongst the tools of interpretation, but rather to either; look at the matter applying all of the tools available to find a true interpretation - a view he had already cast in *KPMG LLP -v- Network Rail Infrastructure Ltd* [2007] Bus LR 1336 - para 50) - put simply, this would start with the ordinary meaning of the wording of the clause and then cross-check this against the commercial sense of the outcome. If there was an unreasonable outcome then a correction needs to be made to give effect to the parties proper commercial intention of the clause.

Alternatively, he mooted for a correction technique of implying terms, or words into terms, to give business efficacy to a provision so as to, again, give effect to the proper commercial intention the parties had when they agreed the clause. The only way that an unreasonable commercial outcome should be given effect to is where *"only the clearest words would justify the court in adopting it"* [para 158]. He said this at paragraph 115:

> *"In any event, this example provides support for the proposition that, where an ordinary reading of the contractual words produces commercial nonsense, the court will do its utmost to find a way to substitute a more likely alternative, using whichever interpretative technique is most appropriate to the particular task."*

Conclusion

The decision highlights the debate between two principles; the freedom of contract and commercial efficacy. The role that each plays in the interpretation of a contract has now been established in the judgment of Lord Neuberger. In short, what people can be said to have freely agreed to, will usually out-do any assertion that that wording would yield an outcome that lacks commercial efficacy such that it should not be followed. The process of interpreting a contractual term should, in the majority of circumstances, start and end with an assessment of what the ordinary meaning of the language means – only in exceptional circumstances will the Court have to interpret the meaning of the words in a term according to what the parties can be taken to have intended from a commercial point of view.

3. Evolution of Contractual Estoppel

Peekay Intermark Ltd -v- Australia & New Zealand Banking Group Ltd [2006] EWCA Civ 386; Springwell Navigation Group -v- JP Morgan Chase Bank [2010] EWCA Civ 1221; Credit Suisse International -v- Stichting Vestia Groep [2014] EWHC 3103 (Comm)

Introduction

Contractual estoppel is a doctrine (if indeed it is one!) which is relatively modern in its inception. It is presently, therefore, evolving at an ever greater speed than normal, spurred on predominantly by the financial services sector. In the last 15 years the financial sector has become accustomed to considerable 'back-covering' through the drafting of accompanying transaction documents, often referred to as 'Risk Management Policy' or words of a similar nature. Essentially these documents purport to set out the factual basis on which a transaction is being entered into and sets out the nature of the relationship between the parties together with the risk which coincides with the transaction in question. As deals have gone south for investors in times of financial turmoil claims have been prompted against the financial institutions who facilitated the transactions normally on the basis that the transaction or its associated risk was misrepresented or improperly advised to the investor. In such claims, reliance on the documentation signed by the parties which set out the factual position and understanding of the parties at the time the contract was entered into, have become of paramount importance.

It is against that background that the doctrine of contractual estoppel was invoked and came into being. The landmark decision of *Peekay* gave birth to the doctrine. Since then it has been developed and evolved in subsequent decisions as its limitations and boundaries have been tested.

The Cases

1. Peekay

P was an experienced investor involved in derivatives. It approached ANZ to effect a transaction based upon the valuation of then Russian Government Bonds known as GKO's. The investment product at that time looked a profitable one as the value of the bonds were high. At the outset P signed various documentations pursuant to the contract governing the transaction. They included Terms and Conditions which governed the nature of the transaction and set out in clear terms what the product was and what it was not.

Towards the late 1990's the value of the bonds plummeted and the investment became worthless. P sued for damages for misrepresentation on the basis that ANZ had not told him the true nature of the investment. In particular he placed reliance on pre-contractual discussions with ANZ regarding whether or not a proprietary right in the GKO's was afforded as part of the investment. The terms and conditions stated that no such right existed – but at the time ANZ's employees when discussing the deal had indicated to the contrary. ANZ relied on the

terms and conditions which had been signed as prevailing over anything which P was now saying he had now been advised of. They clearly set out the nature of the product and gave a definitive answer to the issue now under scrutiny. On the basis of those documents it was argued that P was now estopped from asserting that any other factual basis for the transaction being entered into prevailed.

At first instance P was successful. On appeal however, Moore-Brick LJ held that the terms and conditions were central to the issue and great weight and reliance should be given to them. They were clear and properly signed. In those circumstance it was held that any claim that P had been induced to enter into it on the strength of the misrepresentations could not be sustained. Crucially he held at paragraph 56:

> *"There is no reason in principle why parties to a contract should not agree that a certain state of affairs should form the basis for the transaction, whether it be the case or not. For example, it may be desirable to settle a disagreement as to an existing state of affairs in order to establish a clear basis for the contract itself and its subsequent performance. Where parties express an agreement of that kind in a contractual document neither can subsequently deny the existence of the facts and matters upon which they have agreed, at least so far as concern those aspects of their relationship to which the agreement was directed. The contract itself gives rise to an estoppel…"*

2. Springwell

This is another case based on the derivatives market and the crash of GKO's. This time however, S brought a claim based on the lack of advice which JPC had given to it over the investment and particularly the risk of the GKO market crashing as it did and rendering the investment worthless.

Again, there was documentation signed by the parties at the time that the contract was entered into setting out their respective positions, the nature of the product and the risk associated with the investment. Though the documentation set out that JCP was not acting in the capacity as an adviser to the investment for S, S nonetheless argued that at the time they entered into the contract, JCP's representatives had acted in an advisory capacity by informing them of the product and its nature.

The Court followed *Peekay*. A distinction was drawn between representations given by investment advisers and salesman. The latter applied in this case – the initial conversations regarding the product and the investment were made by JCP representatives in the course of them selling S the investment product, they were not pieces of investment advice. The true position was reflected in the documentation signed at the point of agreement and that categorically outlined that JCP were not obliged to provide any investment advice to S. The Court again held that S was estopped from asserting that another factual basis existed.

In addition, Aikens LJ outlined that contractual estoppel was different from other forms of estoppel. In particular [558-563]:

- There is no requirement to show detrimental reliance.

- It arises on the basis of the contract alone – provided the contract is valid, contractual estoppel can be invoked upon it.

- The party raising estoppel does not need to show that it would be unconscionable for the other party to go back on the assumed state of affairs it had previously accepted.

- The underlying principle is freedom of contract.

3. Credit Suisse

Another derivatives case – this time involving an interest rate swap agreement. CSI contracted with SVG for the swap of interest rates on loans. SVG was a housing authority based in Holland which was governed by its own company constitution. That constitution provided that SVG could enter into hedging transactions. A total of 9 transactions were entered into which were all different to one another. Crucially only 2 of the 9 were found to be properly characterised as hedging transactions.

At the time of the individual agreements being signed and entered into, SVG also signed a Master Agreement in which they warranted that they had capacity to enter into the transactions which flowed under it.

SVG defaulted on the loans and could not provide a security. CSI issued a claim for its losses under both the Master Agreement and individual transaction agreements SVG had defaulted on. SVG claimed that it did not have capacity to enter into agreements 3-9 due to its constitution and the fact that they were not hedging transactions. They therefore argued that those agreements were ultra vires on the basis of lack of capacity and thus any representation made to the contrary regarding capacity within them could not provide a basis for contractual estoppel.

The Court held that the Master Agreement was a valid contract which SVG had capacity to enter into. The warranties made therein as to the capacity which SVG had to enter into transactions under that agreement was an assertion of the factual basis of the agreement in the future. Andrew Smith J held at paragraph 308:

> *"In his formulation of the doctrine of contractual estoppel in Peekay Moore-Bick LJ said that parties are able to agree upon "a state of affairs [that] should form the basis for the transaction". In most of the subsequent cases that have considered the doctrine, the parties had agreed about a present or past state of affairs and made their contract on the deemed basis that that state of affairs obtained or had obtained. But I can see no reason of authority, principle or policy that the doctrine should be confined to agreements of that kind, or that the law should adopt a different approach where parties have made an agreement about a state of affairs in the future, whether or not the label contractual estoppel should be attached in*

> *those circumstances. Indeed, all three considerations seem to me to indicate that the doctrine should not be so confined."*

That caused him to hold at paragraph 315:

> *"I conclude that the parties must be understood to have intended that by the Additional Representations Vestia should warrant that any future transactions that their officers (including Mr de Vries and Mr Staal) purported to make under the Master Agreement would be in accordance with their articles of association. The obvious purpose of the Additional Representations and the mischief that, to my mind, they were clearly designed to meet were that future transactions (or purported transactions) should not be vitiated because of limitations in Vestia's articles of association or Financial Regulations or other applicable laws or regulations. The parties agreed that Credit Suisse should be protected from this risk. After all, the contractual context was that Vestia had provided their articles of association to Credit Suisse, and both parties are to be taken to have entered into the Master Agreement in the knowledge of the limitations on Vestia's capacity with regard to transactions of the kind that might be made under the Master Agreement. (Indeed, it is apparent from the advice of A&O Amsterdam and Mr Tulkens' email that Credit Suisse were so aware.) The fact that the parties included a specific hedging provision leaves no doubt that this concern was the target of the Additional Representations. I cannot accept that the parties contemplated that they would apply only where breach of the compliance provision in relation to a proposed transaction did not make it invalid: where there was nevertheless a valid contract. That, it seems to me, would be to attribute an absurd intention to the parties."*

On that basis, contractual estoppel could be invoked and the Master Agreement enforced as though the individual transaction agreements had been validly entered into by SVG.

Conclusions

Though still in its infancy the doctrine of contractual estoppel is already an important one. This is particularly so in relation to investment claims arising out of failed investment products.

The doctrine is designed so that where the parties made a record of their factual understanding of the contract at the point of agreement, it cannot be altered, or another state of understanding asserted, later on. Contractual estoppel does not merely apply to a factual statement as to past and present affairs but can also apply to a future state of affairs as a result of *Credit Suisse*.

The basis for the doctrine is the contract it arises out of – if that contract is invalid, contractual estoppel will not arise. Furthermore, the doctrine differs from other forms of estoppel and is far easier to invoke as a consequence.

There are two limits to the doctrine: Firstly, the doctrine is constrained by the words setting out the factual background – it cannot go beyond what they say and bolt-on facts cannot be added in. Secondly, it is vitiated by statute and policy.

The interesting point of the future is the extent to which the doctrine will be raised in a context outside of the financial services claims and to claims brought by ordinary non-commercial parties. It has already been invoked in the employment context in the case of *Dinsdale Moorland Services -v- Evans [2014] EWHC 2 (Ch)*.

4. Incorporation of Arbitration Clauses

Barrier Ltd -v- Redhall Marine Ltd [2016] EWHC 381 (QB)

The Facts

R was contracted by BAE Systems for the construction of 6 Astute Class Submarines for the MOD in 2001. In 2002 R sub-contracted the painting of the boats to B. That sub-contract was in relation to Boats 1-3. The contract was then extended to cover boats 4-5 in a meeting in 2012 which had been minuted in writing. By oral instruction thereafter B was also given the work to be done on Boat 6 – this was never recorded in writing.

B claimed that substantial sums had been deducted by R in respect of payment of work done by them. It was accepted that it was a term of the sub-contract that any deduction in monies made by BAE to R for work done under the sub-contract would be passed on by R to B. B did not know if these deductions had been made by BAE or by R unilaterally. They therefore brought an application for Pre-Action Disclosure of that information.

R opposed the application on the basis that there was an arbitration clause incorporated into the contract via one of two routes:

(i) R's own standard terms and conditions, which were normally included on the reverse of purchase orders contained an arbitration clause at clause 18. B had been sent such a purchase order in 2001 and clause 10 of the sub-contract expressly incorporated those standard terms and conditions into the sub-contract.

(ii) In any event, clause 19 of the main contract between BAE and R (which B was not a party to) was an arbitration clause. Clause 10 of the sub-contract expressly incorporated the terms of that main contract into the sub-contract.

B accepted that it had been sent the purchase order in 2001. However, it became clear that the wrong bit of the purchase order had been sent and therefore the terms and conditions usually contained on the reverse had not been sent.

The Decision

HHJ Behrens (sitting as Deputy of the High Court) placed great reliance on the decision of Christopher Clarke J in *Habas Sinai -v- Sometal [2010] EWHC 29 (Comm)* in which he had said at paragraphs 46 and 49:

> *"46. Where parties are in dispute as to what they have agreed the task of the Court is to determine from the communications that passed between them in the context in which those communications were made what reasonable persons in their position would regard them as having intended to agree. Where those parties agree the essential terms of a contract and also that their contract shall include the terms of a previous contract or contracts between them the Court may have to determine which provisions of which contract(s) they meant to incorporate. If the Court is able to decide what those provisions were, it should not, in my judgment, be astute to impose any special rules which limit the ability of the parties validly to agree what, on ordinary principles of construction, they would be taken to have agreed.*
>
> *49. There is a particular need to be clear that the parties intended to incorporate the arbitration clause when the incorporation relied on is the incorporation of the terms of a contract made between different parties, even if one of them is a party to the contract in suit. In such a case it may not be evident that the parties intended not only to incorporate the substantive provisions of the other contract but also provisions as to the resolution of disputes between different parties, particularly if a degree of verbal manipulation is needed for the incorporated arbitration clause to work. These considerations do not, however, apply to a single contract case…"*

That caused Judge Behrens to hold at paragraph 25:

> *"Thus it can be seen he distinguished between the case where there are only two parties involved where no special rules apply and the case where the attempt is to incorporate an arbitration clause between two other parties or one of the parties and a third party. In that situation there is a particular need to be clear that the parties intended to incorporate the arbitration clause."*

That approach led to two different conclusions given the factual and contractual matrixes which were present. As to the incorporation of clause 19 in the main agreement, the wording of clause 9 of the sub-contract was not sufficiently clear to incorporate that clause.

However, as to incorporation of the arbitration clause in R's standard terms and conditions, notwithstanding that they had not been received by B:

> *"I am content to assume (without deciding) that the purchase order sent to Barrier had no conditions on the back. For some unexplained reason the wrong copy was sent or given to Barrier. However a reasonable person reading clause 10 of the subcontract would have no doubt that CIL's standard terms*

were incorporated. The fact that they were not on the back of the purchase order does not affect this. It would, at all times have been open to Barrier to request a copy of the terms if they had wanted to."

As to Boats 4-5 consideration termed to section 5 of the Arbitration Act 1996:

4. *Agreements to be in writing.*

(1) The provisions of this Part apply only where the arbitration agreement is in writing, and any other agreement between the parties as to any matter is effective for the purposes of this Part only if in writing.

The expressions "agreement", "agree" and "agreed" shall be construed accordingly.

(2) There is an agreement in writing—

(a) if the agreement is made in writing (whether or not it is signed by the parties),

(b) if the agreement is made by exchange of communications in writing, or

(c) if the agreement is evidenced in writing.

(3) Where parties agree otherwise than in writing by reference to terms which are in writing, they make an agreement in writing.

(4) An agreement is evidenced in writing if an agreement made otherwise than in writing is recorded by one of the parties, or by a third party, with the authority of the parties to the agreement.

(5) An exchange of written submissions in arbitral or legal proceedings in which the existence of an agreement otherwise than in writing is alleged by one party against another party and not denied by the other party in his response constitutes as between those parties an agreement in writing to the effect alleged.

(6) References in this Part to anything being written or in writing include its being recorded by any means.

The Judge held that the minutes of meeting in which the work for Boats 4-5 was commissioned satisfied section 5(2).

The work for Boat 6 was not in writing but it was accepted by B that it was done under the same terms as the other boats and the sub-contract generally. On that basis section 5(3) was deemed satisfied.

Conclusion

Particular attention is given to the incorporation of arbitration clauses. However, the only requirement for such clauses comes, in reality, from section 5 of the 1996 Act. Once the clause is evidenced in writing, the usual principles of incorporation of terms applies. If the clause is contained in standard terms then physical possession of them, or even the reading of them, is not required so long as they are ascertainable and their existence and incorporation notified to the other party one way or another. Where the clause is said to be incorporated by reference to another contract of which only the party asserting the interpretation is privy, incorporation will only occur where there are clear words to that effect.

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