Case No: HT-2017-000106
Neutral Citation Number: [2017] EWHC 2450 (TCC)

IN THE HIGH COURT OF JUSTICE
QUEEN'S BENCH DIVISION
TECHNOLOGY AND CONSTRUCTION COURT

Royal Courts of Justice

Strand, London, WC2A 2LL

Date: 11/10/2017

Before :

MRS JUSTICE JEFFORD DBE

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Between :

Merit Holdings Limited **Cla**

- and -

Michael J Lonsdale Limited **Defe**

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- -

Justin Mort QC (instructed by **Mills & Co**) for the Claimant

Alexander Hickey QC (instructed by **Stevens & Bolton LLP**) for the Defendant

Hearing date: 22 June 2017

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Judgment

MRS JUSTICE JEFFORD DBE

Introduction

1.
This claim arises out of the construction of One Angel Court, Copthall Avenue, London EC2. The Defendant ("MJL") was engaged as mechanical services sub-contractors. The Claimant ("Merit") describes itself as a specialist contractor.

2.
The hearing before me was of a Part 8 Claim seeking a declaration "as to the correct interpretation of the contract". I will say something more about that Claim in due course but I start by setting out the background.

The facts and background

3.
It is common ground that the parties' initial contractual relationship was set out in a letter of intent dated 20 November 2015 ("the first letter of intent") sent by MJL to Merit. That letter provided:

“We refer to our recent discussion regarding the supply and installation of the mechanical pipework package, pending execution of our formal contract with Merit Holdings Ltd., we hereby confirm by way of LOI expenditure authority / appointment for you to undertake the off-site prefabrication of materials for LTHW, Condenser Water and CHW system and commencement of the on-site installation works for the above mentioned project to a capped value of **£330,000.00.**

….

In relation to any works properly carried out by you in accordance with this letter, we agree to reimburse you the costs wholly and necessarily incurred by you pursuant to this letter up to a maximum sum of **£330,000.00.** (Three Hundred and Thirty Thousand Pounds and Zero Pence). Such costs shall be paid in accordance with MJ Lonsdale payment procedures to be agreed and shall be subject to retention of 0%. This maximum sum shall not be exceeded except where specifically notified to you in writing and any costs incurred by you in excess of such sum shall be borne by you. This letter will expire Thursday 31st December 2015 and another LOI will have to be issued in its place if the formal sub-subcontract order is not in place.

…

In the event that a binding contract is entered into by the parties, all work authorised by Michael J Lonsdale and carried out by Merit Holdings Ltd. pursuant to this letter shall be treated as work performed under the Sub-subcontract Agreement for mechanical pipework services installation. Any monies paid to Merit Holdings Ltd. in respect of this letter shall form part of the Contract Sum under the Sub-Subcontract Agreement.

We may terminate these arrangements at any time by notice in writing to you in which case you shall forthwith vacate the site and leave your work in a safe and secure condition as appropriate, we will pay you, subject to the maximum sum referred to above, the costs accrued due under this letter, up to the date of such termination. We shall have no further obligation or other liability to you in relation to the Works or this letter and you will have no claim against Michael J Lonsdale or any party for any breach or loss of contact (sic), loss of profit, loss of expectation, consequential loss or any other indirect loss in the event that a binding contract does not come into existence.

By your acceptance of the terms of this letter, you acknowledge that there is no contract between us, except as set out in this letter.”

The letter was countersigned on behalf of Merit under the words “We hereby confirm our agreement to commence and complete the Works in accordance with the terms of this letter …”

4.
A further letter of intent (“the second letter of intent”) was sent on 16 February 2016 (incorrectly dated 2015). It was in the same terms as the first letter of intent except that the date of expiry was given as Thursday 29 February 2016. There was obviously a gap in time between the expiry of the first letter of intent and the sending of the second but work continued.

5.
A yet further letter of intent was sent on 6 April 2016 (“the April letter”). It was again in the same terms as the first letter of intent, except that (i) the capped value or maximum sum referred to was £430,000 and (ii) the date of expiry was Friday 29 April 2016. There was again a gap in time between the expiry of the second letter of intent and the sending of the April letter when work continued.

6.
It was Merit's case, as pleaded, that these letters of intent were the basis of the parties' contractual relationship but that "in addition the parties' conduct, including the conduct of the parties after 29 April 2016, varied and/or created the contractual relationship."

7.
It was not in issue that after 29 April 2016, Merit continued to carry out work until 12 July 2016. Between December 2015 and June 2016, Merit made 7 applications for payment. The applications were made roughly on a monthly basis and, therefore, continued during the gaps between the letters of intent. Each application was based on Merit's Tender Summary and assessment of percentage complete against each item. The Tender Summary aligned with a Quantified Schedule of Rates (QSOR) which was provided by Merit under cover of an e-mail dated 3 May 2016.

8.
By the time of the application dated 24 February 2016, the amount claimed had already exceeded the maximum amount of £330,000. The application dated 20 April 2016 was in a sum in excess of £800,000. MJL issued payment notices and made payments which, in due course, exceeded the cap identified in the letters of intent. For the period of the end of April 2016, MJL's gross valuation was £612,974.15. For the period to the end of May 2016, MJL's gross valuation was £813,967.49.

9.
By letter dated 12 July 2016, MJL terminated the arrangement between the parties. MJL's letter was headed Notice of Determination of the Sub-Subcontract. It purported to apply the provisions of clause 26 of the Sub-Subcontract and to terminate the Sub-Subcontract because of Merit's persistent failure to proceed regularly and diligently with the sub-subcontract works. It intimated a claim against Merit in respect of costs incurred in completing the sub-subcontract works.

10.
A dispute arose about payment of Merit's application no. 7 dated 22 June 2016 and, following the termination, in September 2016, Merit commenced an adjudication claiming the sum of £1,128,106.42. The adjudicator, Mr Matt Molloy, decided that the parties' conduct evidenced an agreement that Merit would make applications for payment valuing the work up to the end of each calendar month (amounting to a payee's notice); that s. 110B(4) of the Housing Grants Construction and Regeneration Act 1996 (as amended) was engaged; and that MJL was obliged to pay the notified sum of £1,128,106.42.

11.
In January 2017, Merit made a further application for payment (application no. 8). For the first time, the application was made on the basis of costs allegedly incurred by Merit. On this basis, Merit claimed a further £187,980.87. MJL disputed Merit's entitlement to payment and Merit commenced a second adjudication in which the adjudicator was again Mr Molloy. In the adjudication, Merit sought payment. In the alternative, Merit sought a declaration as to the basis on which its entitlement to payment was to be calculated. Its case was that it was entitled to be reimbursed its costs wholly and necessarily incurred, in accordance with the terms of the letters of intent.

12.
In his decision, Mr Molloy set out the evidence before him including that as to Merit's tender, the minutes of a Pre-Order Meeting on 25 August 2015, and the fact that applications for payment nos. 1 to 7 were all based on the tender summary and a Contract Sum Analysis signed by Merit on 17 March

2016. In his decision dated 20 April 2017, he decided that Merit was not entitled to the sum claimed and that its entitlement to payment was based on the agreed Contract Sum and the QSOR.

13.
Given what I say below about the contractual relationship, it seems to me helpful to set out the material part of Mr Molloy's analysis and decision in full:

"In Adjudication No. 1, I accepted that the parties' contractual relationship continued after the expiry of the 6th April 2016 letter of intent, i.e. after 29th April 2016. By that date, the parties had evidently agreed a Contract Sum and a scope of work, but a formal contract had not been concluded or terms agreed. The fact that Merit submitted subsequent applications for payment based on the agreed scope of works and the agreed Contract Sum, and the fact that MJL had made payments based on that agreed scope and Contract Sum points heavily towards the conclusion that the parties are taken to have agreed by their conduct that the basis of payment after the expiry of the 6th April 2016 letter of intent was by reference to the agreed Contract Sum and the QSOR. Alternatively, I also consider there to be some force in MJL's submission that, if there was no formal agreement regarding the basis of payment following the expiry of 6th April 2016 letter of intent, then Merit would be entitled to a quantum meruit to be valued by reference to the Contract Sum which had been agreed. My view is that either analysis is consistent with the basis upon which Merit advanced its case in Adjudication No. 1 and the Decision reached.

Accordingly, I find that the basis of Merit's entitlement to payment is to be based on the agreed Contract Sum and the QSOR."

14.
On the same date as Mr Molloy's decision, MJL gave notice of intention to adjudicate. The notice stated that the adjudicator would be asked to value application no. 8 and make declarations in relation to "the final account".

15.
On 27 April 2017, Merit issued the Part 8 Claim Form that gave rise to these proceedings.

16.
At the time of the hearing, I was not made aware of the progress of this adjudication.

Procedure

17.
I make a number of points about the procedure that was adopted in this case.

18.
Firstly, under section 9 of the TCC Guide, dealing with Adjudication Business, paragraph 9.4.1 notes that the Court will deal with applications for declaratory relief arising out of the commencement of an adjudication. Common examples given are disputes over the existence of a construction contract, the jurisdiction of the adjudicator or the scope of the adjudication. Paragraph 9.4.2 contemplates directions leading to a "speedy resolution" of the proceedings (in common with the abridged directions that are given in adjudication enforcement cases). The point here is that the Court will act quickly where there is an issue that goes directly to the proper constitution of the adjudication at its commencement.

19.

Although there was an adjudication background to this Claim, it was not a Claim which directly related to the commencement of an adjudication in the sense used in paragraph 9.4.1. What the Details of Claim said was that the adjudicator had been wrong in his decision about the basis of payment because the agreement between the parties was that “the basis upon which the Claimant’s entitlement was to be calculated after termination was by reference to the costs wholly and necessarily incurred by the Claimant.” In other words, the Part 8 proceedings related to the substance of the decision in the adjudication. The Details of Claim further averred that the same error was now being “promulgated” in adjudication no. 3.

20.
When the matter first came before the Court, however, it was presented as if it was an adjudication matter and an application was made for directions “pursuant to paragraph 9.4.1 of the TCC Guide” and in accordance with paragraph 9.2. That has, and had, consequences for the manner in which the case is dealt with by the Court, directions, listing and time estimates, and allocation of Court resources. In this case, directions were given leading to a hearing less than 2 months later. An explanation was provided for why this course had been taken in this particular case and I recognise that there may be instances in which it makes no sense for there to be a series of adjudications on an erroneous basis such that the Court, if an appropriate application were made, might be minded to list a hearing promptly to avert unnecessary cost and expense. But I take the opportunity to emphasise the guidance in the TCC Users’ Guide paragraph 9 as to the type of applications for declaratory relief that will be dealt with as “Adjudication Business” and in accordance with paragraph 9.2. It should not be assumed that some relationship to an adjudication and an adjudication label means that it is automatically appropriate for a case to be dealt with in this way.

21.
Secondly, and more generally, subject to CPR Part 8.1(6), the Part 8 procedure is to be used where the claimant seeks the Court’s decision on a question which is unlikely to involve a substantial dispute of fact. Part 8.2 provides that the Part 8 Claim Form must state “the question which the claimant wants the court to decide; or the remedy which the claimant is seeking and the legal basis for the claim to that remedy”. It is, therefore, an express requirement of the use of the Part 8 procedure that the question for the Court is one that is unlikely to involve a substantial dispute of fact and it is, it seems to me, to be implied in the rules that the question should be framed with some degree of precision and/or be capable of a precise answer.

22.
The experience of this Court shows that there is a real risk of the Part 8 procedure being used too liberally and inappropriately with the risks both of prejudice to one or other of the parties in the presentation of their case and of the court being asked to reach ill-formulated and ill-informed decisions.

23.
In this case, MJL’s Acknowledgement of Service took issue with the Court’s jurisdiction on the basis that the Claim involved substantial issues of fact. That was an unsurprising stance given that Merit’s pleaded case turned substantially on what it said were the consequences of or inferences to be drawn from the conduct of the parties rather than, for example, from words used. By the time of the hearing before me, MJL’s position had shifted. MJL no longer maintained a jurisdictional objection as such and considered that it may be useful for the Court to reach decisions which could resolve issues between the parties. MJL recognised, however, that the Court might still have reservations about that approach.

24.
I did indeed have such reservations and it remains, of course, a matter for the Court's discretion whether to grant declaratory relief at all.

25.
Despite the characterisation of the question for the Court as the correct interpretation of the contract, this is not a case in which the Court is being asked to construe the written terms of the contract. On the contrary, the Court is being asked to determine the very nature of the contractual relationship between the parties, both parties accepting that there is some contractual relationship. It is highly unusual for the Court to be asked to do so, in effect, on documents only with a short hearing. My concerns were allayed to a large extent by Mr Mort QC's submission that the relevant facts were short and uncontentious and that MJL had not identified any other factual issues on which it might wish to rely. This is important: it is only in such cases that it is appropriate to issue Part 8 proceedings.

26.
I remained concerned, nonetheless, about the scope of what the Court was being asked to do and I heard this Claim on the basis that I would not reach a conclusion until giving judgment as to how far I should go in terms of findings or declarations. There were a number of unsatisfactory aspects of these proceedings which did not make this task easier and serve to emphasise why the Part 8 procedure should not be over liberally deployed.

27.
As I have said, Merit's Claim Form asked the Court to make a declaration as to the correct interpretation of the contract. That is not as broad a declaration as may at first blush appear because I accept that it has to be read in the context of the dispute and arguments identified in the earlier paragraphs of the document, including that quoted at paragraph 19 above. From this context, it appeared that the declaration sought was that "the basis on which the Claimant's entitlement was to be calculated after termination was by reference to the costs wholly and necessarily incurred by the Claimant." At the oral hearing, Mr Mort QC, on behalf of Merit, formulated for me the declaration he was seeking as "The Claimant is entitled to be paid its costs wholly and necessarily incurred on the project" and he clarified that he sought that declaration in respect of all works carried out.

28.
Where a Defendant to Part 8 proceedings disputes the terms of a declaration sought by the Claimant, it is not, in my view, incumbent on him to proffer an alternative declaration. If he were, the Claimant would, in effect, be able to compel the Defendant to seek declaratory relief that he does not in fact want to seek. The effect of that here was that, although MJL were content for the Court to reach decisions that might assist the parties, there was no formulation of any declaration that MJL sought.

29.
Mr Mort QC offered a formulation of the appropriate declaration in his oral submissions as "The Claimant is entitled to be paid by reference to rates tendered by the Claimant and the Claimant's Quantified Schedule of Rates." Mr Hickey QC, for MJL, in his skeleton argument invited the Court to "make clear in its judgment that the only basis of any entitlement to payment now, post termination (whether by way of simple basic contract or a quantum meruit), is to be by way of valuation for the works carried out by Merit up to July 2016 in accordance with the Contract Sum/QSOR on a final payment basis." The alternative bases reflected the different possibilities as to the contractual position which the adjudicator had also alluded to.

30.
Mr Hickey QC left me a number of options as to whether I gave declaratory relief and in what terms or whether I expressed views as to the true position without deciding it. The latter option seems to me largely unsatisfactory – any such views would be persuasive only and the court is there to make decisions not express non-binding opinions which may well store up trouble for later both as to their status and content.

31.
Had a Part 7 procedure been adopted, then on the face of the pleadings, the parties' positions would have been fully set out and, if not, further information could have been sought. If there were no need for factual evidence, there would have been mechanisms available (in the discretion of the court) to resolve the issue of the contractual relationship between the parties promptly – for example, by the hearing of a preliminary issue or an expedited hearing – and on a surer footing than is offered by the Part 8 procedure in circumstances such as this.

32.
All these issues seem to me to illustrate why care should be taken by the parties and the Court in the deployment of the Part 8 procedure.

Analysis

33.
Against that background and bearing in mind my own reservations, I turn to the issues.

34.
The April letter clearly stated that it would expire on 29 April 2016. It is equally clear that the works continued after that date. Neither party contends that that happened on anything other than the basis of a contract between the parties.

35.
I can summarise the parties' competing positions as follows:

(i)
Merit says that the conduct of the parties after that date evidences an agreement to extend the application of the letter of intent beyond the expiry date and without regard to the cap on payment. Under the terms of the April letter, following termination, Merit was entitled to be paid its costs wholly and necessarily incurred for all the works carried out until it ceased work.

(ii)
MJL disputes this. Mr Hickey QC says that the conduct of the parties evidences an agreement to carry out the works on the basis of a simple contract in which the scope of works and price was agreed. That contract is one for the whole of the works (not just those works carried out after 29 April).

36.
Merit's case turns on what it can objectively be inferred the parties agreed should happen after 29 April 2016. For the reasons I explain below, I cannot accept what Merit submits the parties did agree and it seems to me to bear no relationship to the reality of the situation.

37.
Up until 29 April 2017, and despite what the letters of intent said about payment of costs, Merit had applied for, and MJL had made payments based on, the valuation of the works (not cost). After 29

April 2016, that continued to happen by the applications made for the periods to the ends of May and June. On that basis – that is that what was being paid was the value of the work - the amounts paid exceeded the cap.

38.
Merit's argument is that what the parties can be taken objectively to have agreed is that (i) the expiry date was extended and (ii) the cap was removed. As Mr Mort QC put it in his skeleton argument, the parties continued after 29 April 2016 "precisely as before, save that they necessarily disregarded the requirement for a further letter of intent and they also disregarded the agreed cap contained in the last letter of intent". He described these as "modest modifications" to the agreement in the April letter and submitted that that agreement was to be inferred because it made the fewest amendments to the agreed written terms. Since in all other respects the written terms of the letter of intent remained in force, Merit was entitled to payment of costs. Merit argued that it was irrelevant (or at the least explicable) that it had previously made applications for payment on the basis of a percentage completion of a defined scope of works valued as a percentage of a contract price. This was simply a mechanism for valuing interim payments in anticipation of a contract (for that contract price) being entered into.

39.
Merit's argument ignores two material matters:

(i)
Firstly, it is inherent in that argument that the parties must be taken to have agreed to remove the cap on the sums to be paid for costs wholly and necessarily incurred. There is not a shred of evidence to support that proposition. The only evidence is of applications for payment being made for the value of the works in excess of the cap and such payments being made. The most obvious inference to be drawn from the continuation of that conduct after 29 April 2016 is indeed that they continued on the same basis as before – namely that payment would be made for the value of work done (necessarily exceeding the cap). That is consistent with the conduct of the parties throughout the project including in the periods between the letters of intent. Merit argued that the obvious inference during these gaps was that the parties had agreed to continue under the terms of each of the letters of intent despite their expiry and thus on the basis that Merit was entitled to be paid costs wholly and necessarily incurred but, at no point, did Merit apply for or receive payment on this basis. I can thus see no basis for concluding from the parties' conduct after 29 April 2016 that what they had agreed was that payment should be made for work done on a costs basis in excess of the stated cap.

(ii)
Secondly, the terms of each of the letters of intent, including the April letter, required the parties to agree in writing if the cap was to be exceeded. It is, of course, right that payment was made of greater amounts but they were a percentage of a putative contract sum not costs. It seems to me to go too far to infer that the parties had agreed to dispense with the requirement to agree in writing if the cap was to be exceeded for payment on the basis of costs incurred and is inconsistent with Mr Mort QC's "least damage" argument.

40.
Further, I do not accept, as Merit submits, that the fact that all payments were applied for and made on a percentage complete/ valuation basis can just be dismissed as an interim payment mechanism. As Mr Hickey QC submitted, the commercial purpose of a letter of intent is to enable the employer/ contractor to have work carried out before a contract is entered into and it gives the contractor (or, as

in this case, the sub-subcontractor) an entitlement to payment or at least comfort as to payment for costs incurred and work done before the contract is entered into. A maximum amount payable will commonly be included for the protection of the employer/ contractor. That is what happened here and the commercial sense of that is self-evident.

41.
In this case, however, the parties had already agreed a contract sum. So it did indeed, as Mr Mort QC submitted, make sense for Merit to be paid on the basis of the putative contract sum both before and after 29 April 2016 because it was anticipated that a contract would be concluded for that sum. If, as Merit argued, this was simply a matter of convenience, and Merit had sought payment on a costs basis instead, then up until the expiry of the last letter of intent, its recovery would have been capped. Moreover, if a contract had been entered into, then, as the letters of intent each provided, the monies paid would form part of the Contract Sum. I take that to mean that they would count towards payment of the Contract Sum. In neither of these circumstances would there be an open-ended liability of MJL to pay Merit's costs wholly and necessarily incurred. Why then would MJL suddenly and silently (and ignoring the express terms of the letters of intent) have agreed on 30 April 2016 that the cap on the payment of costs incurred was swept away and Merit's entitlement to recover its costs was unlimited in respect of works carried out both before and after April 2016? I can think of no sensible answer to that question and, construing the conduct of the parties, I find it impossible to conclude that that is what was agreed.

42.
In my view, the far more obvious interpretation of the parties' conduct is that they agreed that Merit would continue to be paid (in excess of the cap) on the basis of the contract sum – that is a commercially sensible agreement because the contract sum is, in a sense, its own cap and one agreed by the parties to reflect the value of the work to be done.

43.
It is, therefore, in my judgment, quite clear that the Claimant is not entitled to the declaration as formulated by Mr Mort QC and I so find.

Alternative declarations?

44.
The correlative of this would, at first blush, seem to be that I could and should make the declaration as to MJL's case that was formulated at paragraph 29 above or give the clarification MJL sought. The difficulty with those options is that I would be making a positive declaration as to the basis of payment without, if I go no further, deciding the underlying contractual relationship. So I ask myself whether I should go further and reach any other binding conclusions or make any declarations about the parties' contractual relationship.

45.
I have already indicated that the parties' conduct evidences some agreement that Merit should continue work and would be entitled to be paid the value of that work rather than cost. There are I think multiple possible views of that position contractually:

(i)
the letters of intent governed work up to 29 April 2016 but with payments made on the basis of the valuation of the works. After 29 April 2016, the parties agreed to continue on the basis of the April letter but still with payments made on the basis of the valuation of the works. Under such an

arrangement, there would be no obligation on Merit to carry out and complete any defined scope of works and no entitlement to do so.

(ii)
The letters of intent governed work up to 29 April 2016 but with payments made on the basis of the valuation of the works. Thereafter there was a fresh agreement in respect of work after that date. That agreement was that Merit would carry out works as requested or instructed which were to be valued and paid by reference to the contract sum (and were not subject to the cap in the April letter). Under such an arrangement, there would similarly be no obligation on Merit to carry out and complete any defined scope of works and no entitlement to do so.

(iii)
The letters of intent governed work up to 29 April 2016. After 29 April 2016, there was a “simple” contract pursuant to which the balance of the (I am told agreed) scope of works would be carried out by Merit for the agreed contractual sum.

(iv)
After 29 April 2016, the arrangements under the letters of intent were replaced by a “simple” contract for the whole of works for the contract sum.

(v)
After 29 April 2016, there was a contract for the whole of the works which incorporated MJL’s standard terms and conditions.

46.
There may be other interpretations of the position. There are a number of material differences in the scenarios I have identified which go not merely to payment but also to alleged breaches and any potential claim by MJL for damages for breach, which has already been advertised.

47.
Although I have been assured by the parties that I have all the relevant facts, the discomfort which Mr Hickey QC anticipated I would feel in reaching conclusions on the contractual relationship between the parties is acute when I am asked to do so in a complete vacuum of information about the circumstances of this project and its progress, which it can readily be seen may be relevant to what the parties agreed in the course of an ongoing project. I have found this issue by no means easy but I have concluded that it would not be appropriate for me to go further in determining the contractual relationship between the parties at this stage.

Conclusions

48.
I therefore refuse to make the declaration sought by Merit as formulated at the oral hearing.

49.
I make no other declarations.

50.
The parties will want to consider how to proceed but I will regard the present proceedings as remaining alive until further submissions from the parties as to their disposal, allowing for the possibility that they be treated as Part 7 proceedings in which the remaining issues can be resolved.