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Dispatch highlights some of the most important legal developments during the last month, relating to the building, engineering and energy sectors.

Dispatch

Architects: advising on budgets

Riva Properties Ltd & Ors v Foster + Partners Ltd
[2017] EWHC 2574 (TCC)

This case has generated a lot of publicity. In short, the Claimants (through "Mr Dhanoa") alleged that Fosters were in breach of the duty owed to exercise reasonable care and skill in their professional performance undertaken between 2007 and 2009 following their engagement as architects to design a hotel at a site at London Heathrow. To resolve this issue, Mr Justice Fraser had to consider the scope of Foster's duty towards Mr Dhanoa and in particular the extent to which they had to ascertain the budget and/or advise their client generally about the budget and whether it was realistic or not.

Mr Dhanoa said that he told Fosters that his budget for this project was £70 million. Fosters embarked upon the design process, and produced a scheme that was costed in February 2008 at £195 million. Mr Dhanoa said that he then increased the budget to £100 million, in reliance upon Fosters telling him that the project could be "value engineered" down to that figure. However, Mr Dhanoa could not obtain funding for the scheme, which he eventually discovered could not possibly be value engineered downwards to as low a figure as £100 million. He could not therefore build the scheme which Fosters had designed for him, and which had cost him approximately £4 million in professional fees. Fosters denied that there was any budget and said that at the least Mr Dhanoa had no budget, or at least none that he had communicated to them. Further Fosters stated that they were not obliged to find out whether he had a budget or not and they were not engaged to provide costs advice;

Mr Justice Fraser found that Fosters, as part of their contract, were clearly obliged to provide the "Full service A-L" which meant all of the RIBA Work Stages. This meant that Fosters were therefore responsible for the identification of key requirements and constraints. A client's budget for a project was plainly a constraint (and also probably a requirement too). If Fosters were obliged to prepare the Strategic Brief (which the Judge said that they were), this would and should have included identification of the budget as a key requirement and constraint. Both the expert architects accepted that in some, if not most projects, the budget can be a constraint. It was therefore necessary for any architect in Fosters' position to establish whether there was a budget or not at an early stage, as that was the only way that all of the key requirements and constraints could have been identified.

Further clause 8.1 of the contract, noted that: "*...the Consultant has used and shall use all the skill, care and diligence to be expected of suitably qualified and experienced architects undertaking services the like of those undertaken by the Consultant in relation to projects of the scale and character of the Development*". The "scale and character of the Development" can only be established if the existence, or absence, of a budget is also established.

Mr Justice Fraser went on to discuss what "the budget" actually was. Obviously, the term can have many different meanings depending upon its context. The Judge said that in the context of this project (if not in all, or at least most, construction projects) "it connotes an approximate outturn cost for the project; it can also mean the approximate level of the funds available to the developer or employer". Here, the meaning given to that phrase by the parties during 2007 and 2008 was the approximate outturn cost for the project. It could only be an approximation, certainly in the early stages of any project. Fosters said that they were architects, not costs specialists, and so could not give costs advice. That was true, but that did not mean that "budget" in the sense that it was used by these parties throughout this project was not relevant. Budget meant the amount of funds available or the amount that one wished to spend. Fosters sought to draw a distinction between a budget used by a professional firm to calculate fees, and a budget for the approximate outturn cost. What they were trying to do was to justify their use of the figure of £75 million to calculate their fees, but at the same time distinguish this from their having to design a building to within even approximate touching distance of that figure as a budget. This approach was firmly rejected.

The Judge made it clear that the brief from Mr Dhanoa was "remarkably simple". He wanted a 500 bedroom 5 star hotel that could be built within the budget on the site he had acquired at Heathrow. The Judge agreed that the budget was not specified in the Fosters' Appointment. The request from Mr Dhanoa to clarify his brief and requirements in the Appointment was simply ignored. However, that did not matter because Stage A required Fosters to identify their client's requirements and possible constraints in any event. This included the budget. Even if the budget had not been communicated to Fosters by Mr Dhanoa, they had an obligation to enquire of their client whether there was a budget, and if so, what it was. That said the Judge was satisfied that the budget was communicated to Fosters. What Fosters could not do was excuse themselves from performing the services required in Stages A and B by saying the budget equated to costs, and costs were nothing to do with them as architect.

In addition to this, Mr Justice Fraser held that Fosters had negligently advised that the project could be "value engineered" down from £195m to £100m. Further, as Mr Dhanoa expected the cost-reduction to happen by value engineering, Fosters were under an obligation to advise him that it could not be done. However as the Judge himself commented, the fact that Fosters had been held to be in breach of their obligations to Mr Dhanoa was but one step along the road to the recovery of damages.

Architects: recovery of losses

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The largest of Mr Dhanoa's claims was for loss of profits on the basis that he was not able to proceed with his scheme because of the advice given (or not given) by Fosters. This claim failed. The breaches by Fosters were not the effective cause of Mr Dhanoa being unable to construct the hotel. The reason the hotel was not built was the lack of funding caused by the financial crash in the period 2007-2009. As a result, whereas previously, the borrowing of very sizeable sums in the tens of millions of pounds (and certainly £100 million) had been widely available now such sums were far less available. Further, the new lending approach post-financial crisis meant that funders required a much greater contribution from the borrower.

The Judge noted that an identical result would have been obtained by posing an entirely different question, namely whether the inability to obtain funding, caused by the financial crisis, was a type of harm from which Fosters had a duty to protect the claimants? That question arose from the 2017 Supreme Court decision in the case of *Hughes-Holland v BPE Solicitors*. The point here was that there was a distinction to be drawn between information provided to a party, and the giving of advice. The Judge did not consider that the professional service provided by Foster, namely the design of the hotel scheme, fell into either category. The professional services encompassed advice in some respects (such as the advice in respect of value engineering) but the scope of the retainer was to design the scheme and provide the architectural services.

Here, Fosters were not engaged to give advice on the business viability of the hotel scheme. To give that advice, any professional adviser would need to consider the financial resources available to the client, the credit risk they would represent to any lender, and other relevant information. This type of advice formed no part of the architectural services which Fosters agreed to provide.

However Mr Dhanoa was able to recover compensatory damages in relation to the amount that was paid to Fosters under the contract. Fosters should have designed to the budget if there had been one, but a failure to do would be what one of the experts called at "architect's risk". By this the expert meant that Fosters could simply be required to do the design again, at their own cost, if they failed to comply with the budget first time around. This essentially came down to an acceptance that an architect must design to his client's brief. Any architect exercising reasonable skill and care would, if a client provides a budget, take that budget into consideration when in designing the project. It cannot simply be ignored.

Looked at another way, the best evidence of how much it would cost the contracting party to have such a design produced by an alternative architect was the cost Fosters were charging to do this. As a result this amount could represent the measure of damages for breach of contract, calculated on an "expectation" basis. It was not recovery of the sums paid to Fosters (and the other professionals) as such, it was using the sums paid to Fosters (and the other professionals) as the appropriate measure of the damages payable to the claiming party, to put it in the position it would have been in, had Fosters complied with their obligations under the contract. It was using those sums as the measure of the expected loss. The same was true of other services. For example, quantity surveying services would be required on the successor scheme and so they would be incurred again. Accordingly they were recoverable from Fosters here.

Pay Less Notices

Muir Construction Ltd v Kapital Residential Ltd

[2017] CSOH 132

This was a Scottish case which came before Lord Bannatyne. Following a lengthy dispute, the parties had agreed a Settlement Contract which was executed on 7/8 April 2016. The contract rectification period ran from 21 July 2015 to 20 July 2016. On 21 December 2016, Kapital issued a pay less notice ("PLN") valuing the sums due to Muir at "zero". The PLN was issued ten days before the retention sum was to be paid by Kapital to Muir pursuant to the Settlement Contract.

Kapital said that following the decision in *Surrey & Sussex Healthcare NHS Trust v Logan* (*Dispatch* Issue 200), a "common sense, practical view" of the contents of a pay less notice should be taken, not "an unnecessarily restrictive" one. Provided that the notice made "tolerably clear" what is being withheld and why, the courts should not intervene.

Here, the PLN included (i) a formal letter from Kapital to Muir on 21 December 2016; (ii) the formal PLN; (iii) a note of outstanding snagging; and (iv) an expert opinion which detailed defects and incomplete works. Where the retention amount was small and a very large amount of work was necessary for defects to be remedied, it was enough to say the remedying of the defects would require a sum well in excess of the retention sum. This was the basis upon which the PLN in this case arrived at "zero".

Muir said that the PLN did not properly specify the basis of the "zero sum". Taking a strict view, the Judge saw some "substantial force" in this argument. No basis for the zero sum figure was put forward in the PLN or the supporting documentation. The Judge noted that:

"From none of the information provided could the reasonable recipient work out the basis on which the zero sum figure was calculated. There is no calculation put forward which would allow the reasonable recipient to understand how that figure is arrived at. There is no specification which would allow the reasonable recipient to make any sense of the figure arrived at. The defender sets forth no figures and thus no basis substantiating the zero sum figure in the PLN or in any of the other documentation upon which it relies.

With no difficulty I reject the defender's response with respect to this point. It amounted to no more than saying the sum retained is not a large one and given the number and nature of problems founded upon in the PLN the cost of remedying these would clearly amount to a figure well in excess of the retained sum and thus a basis for the zero sum figure was provided. That is not providing a basis for the figure. I am persuaded that the PLN in order to properly provide a basis needs at least to set out the grounds for withholding and the sum applied to each of these grounds with at least an indication of how each of these sums were arrived at."

In reaching this conclusion the Judge referred to the case of *Maxi Construction Management Ltd v Mortons Rolls Ltd* (*Dispatch* Issue 15) where Lord Macfadyen had said that: "*specification of the basis of calculation*" was required. There was no specification here. As a result the Judge said that the PLN was neither valid nor effective.

Further as part of the Settlement Agreement, where Kapital had undertaken work to remedy the defects, it could only recover costs where (i) it had already incurred the cost sought to be withheld and (ii) it could evidence that to Muir. This meant that the "mere crystallising of the liability" in terms of invoices becoming due and payable was not sufficient to satisfy the condition of costs having been incurred. To allow this, would potentially allow an invoice which did not, in part at least, represent work actually done and/or where payment was not made timeously but made some material time later, to form the basis for a valid PLN. On the facts here, the proper construction of "costs incurred" for the purposes of a valid PLN was that the sums in any invoices for work done had to have been paid by 21 December 2016.

Dispatch is produced monthly by Fenwick Elliott LLP, the leading specialist construction law firm in the UK, working with clients in the building, engineering and energy sectors throughout the world.

Dispatch is a newsletter and does not provide legal advice.

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