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Dispatch

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

On demand bonds: documents supporting a call

AES 3C Maritza East 1 Ecod v Credit Agricole Corporate Investment Bank & Anr
[2011] EWHC 123 (TCC)

AES sought summary judgment against the defendant bank ("Calyon") in respect of two demands made on an on-demand bond provided to AES under a contract for the construction of a power plant in Bulgaria. The contractors under that contract were two Alstom Group companies. The bond stated that it was independent of the EPC contract and would remain in full force and effect despite any illegality, invalidity, termination, disclaimer or discharge of the EPC contract. The bond was payable "on receipt of a demand" made in accordance with clause 4. The bond was governed by English law and the English courts had non-exclusive jurisdiction over disputes connected with it. Any liability of Calyon to pay under the Bond was subject to an indemnity from Alstom. By 20 December 2010, AES considered that it was clear that Alstom would inevitably fail to achieve the performance required under the EPC contract in relation to unit 1 by the due date of 25 December 2010 and that Alstom would not achieve the performance required in relation to unit 2 by the due date of 31 December 2010.

On 20 December 2010, AES issued a demand for EUR93 million under the bond to Calyon (first demand) which covered both certain existing liabilities and those liabilities that it seemed clear would arise on 25 and 31 December 2010. On 28 December 2010, before a court in France, Alstom obtained interim injunctions preventing Calyon from making payment to AES under the Bond. On 31 December 2010, AES applied for summary judgment in respect of the sum claimed under the first demand. Calyon responded by stating that the demand was ineffective on the grounds that the demand was for €93 million but the documents enclosed with the first demand related to only €27 million. And so on 17 January 2011, Calyon received a second demand from AES, demanding payment of €96,604,166.83. The second demand exhibited letters and invoices in relation to the total sum claimed. To complete the picture, Alstom obtained a second injunction in France and AES issued a second summary judgment application, both in relation to the second demand.

Calyon referred to clause 4(f) of the bond which said that the demand should contain "*any notice to or claim against Contractor [Alstom] relating to the respective breach of its obligations to which the demand refers*". They argued that the claim was made in respect of monies that were not due until 25 and 31 December 2010. Alstom further suggested that the second demand was also invalid because, having made the first demand, any further demand for the same amount of money was invalid.

AES submitted that they were entitled to demand sums which had not yet become due and payable but which, on the evidence were inevitably going to become due and payable within a short period after the demand. In these circumstances, the first demand did contain the necessary statement that Alstom had failed to comply with its obligations under the Contract and AES had supplied the relevant notices or claims relating to the breach relied on.

Mr. Justice Ramsey held that the question of whether there has been a relevant demand under an on-demand bond depends upon the wording of the particular bond. Here he accepted that the bond, like many on-demand bonds, was payable against an appropriately worded demand accompanied by such documents as the demand required and without proof of the existence of a liability under the underlying contract. The issue was whether a claim for sums not yet alleged to be due and payable, and for which there was no notice to or claim, could be demanded under the Bond. The Judge felt that the documents which had to be provided to support the call were those which support the demand which is made for a failure to comply with the obligations of the contract. That requirement did not mean that there had to be any proof of breach of the underlying obligations under the contract.

The only documents which were required were a notice to or claim against Alstom relating to the alleged breach of obligations under the contract which was relied upon by AES in their demand. Given that Calyon were entitled to decide whether or not to pay based upon those documents, he did not consider that there could be a valid demand where, the notices or claims were in respect of some €27million but the claim was made for €93 million. There was therefore no document or claim in respect of the balance of some €66 million. As the demand had to include a statement that Alstom has failed to comply with its obligations in accordance with the contract, the claim had to be based on an assertion by AES that the sum is due and payable by Alstom for the breach of the obligation.

That left the second demand. Here of course the "problem" with the call made the first time round had been corrected. The documentation which was served with the second demand properly supported the sums claimed and conformed to the terms of the Bond. The Judge disagreed with Alstom that having made the first demand, the second was defective because AES could not make another demand for the same sums in circumstances where the first demand had not been withdrawn. As the first demand was invalid, there was only one valid demand – namely the second. Accordingly, the Judge granted summary judgment in the sum of €96,604,166.83 but ordered that the judgment was not to be enforced so long as Calyon was prevented from complying with that judgment by the Order of the French Court.

Damages - consequential loss

McCain Foods Gb Ltd v Eco-Tec (Europe) Ltd
[2011] EWHC 66 (TCC)

This case related to the purchase by McCain of a BGPur system from Eco-Tec under an Equipment Purchase Agreement including a Specification. McCain successfully argued that the System proved impossible to commission successfully and then sought recovery of monies paid under the Contract and damages. Interestingly the single joint quantum-expert had said that:

"Had the Claimant purchased the comparable system rather than the Equipment from the Defendant, it would have incurred the full cost of the system from Treatment Systems Limited (£389,750). Therefore, I consider the only additional costs incurred by the Claimant are the costs expended on the allegedly faulty equipment. As such, my calculation for this category reflects the purchase price of the Defendant's system £224,282."

This approach was rejected by Mr. Recorder Acton Davis QC as being the wrong test.

Eco-Tec accepted liability for the costs of replacement equipment, but not for other costs such as the costs of employees and third parties. Clause 19.1 of Schedule B of the EPA said that:

"... Seller will indemnify and hold McCain and its directors, officers, employees and agents harmless from and against any and all losses, liabilities, damages and expenses whatsoever (in no event however will Seller be responsible for indirect, special, incidental and consequential damages) arising out of any breach by Seller of any commitment or other obligation contained in this Agreement or in any document delivered pursuant hereto or in connection herewith or out of any inaccuracy or misrepresentation of (sic) any representation or warranty made by Seller herein or in any such other document, or out of any actual or alleged injury to persons or property due to the acts or omissions of Seller and those for whom in law it is responsible, whether on the premises of McCain or otherwise".

Eco-Tec said that the remainder of the claim fell within the definition of "indirect, special, incidental and consequential damages". The Judge referred to the case of Hotel Services Ltd v *Hilton International Ltd* [2000] BLR 235 where Hilton rented from HSL a number of mini bars for installation in Hilton Hotels. The rental agreement excluded HSL's liability for any "indirect or consequential loss, damage or liability arising from any defect or failure in the system". The chillers in the mini bars leaked ammonia and the units had to be removed. Hilton claimed, amongst other losses, loss of profit from the use of the mini bars.

The CA held that the loss of profit claim was direct loss with LJ Sedley commenting that:

"An example of consequential loss might be injury to the profitability of the hotel itself. But when the contract is one of hire of the "thing itself" is not the equipment but the use of the equipment, and if through breach of contract it becomes unusable and dangerous the natural or immediate loss is, it seems to us, the profit (if any) which it would otherwise be yielding and the cost of neutralising the danger".

Eco-Tec in particular focused on additional utility costs and the lost revenue from Certificates of Renewable Energy Production (or Renewable Obligation Certificates - ROC's") and maintained that these were consequential costs. The Judge disagreed. The costs of repair, replacement, mitigation and associated losses were direct losses. Eco-Tec were liable too for the costs of contractors, site managers and health and safety personnel, attempted mitigation, auxiliary equipment and civil works, employee time, third party experts and laboratory testing and the purchase of auxiliary equipment from Eco-Tec.

The additional utility costs arose because they are the costs of electricity which McCain had to purchase elsewhere during periods which ought to have been generated by the System. The claim for lost revenue from ROC's arose because the Renewals Obligation Order 2007 created a market for such certificates. An accredited generator of renewable energy can use the renewed energy itself and sell on to another electricity supplier the ROC's issued for the renewable energy produced and used. Thus, had the System been commissioned, McCain would have obtained certificates under the Order which had market value.

When it came to loss of profit, the Judge accepted that this could be direct loss. It seemed to him that the use of the System would have resulted in revenue and that loss of revenue is the natural or immediate and thus direct loss caused by the inability to commission the System. It was argued that the mitigation of loss was overly expensive and thus unreasonable. However the Judge accepted that the evidence before him explained how those costs arose and what was done. In his judgment, set in the context of the losses, those attempts amount to reasonable mitigation of loss.

With employee time, it was argued that there was an absence of contemporaneous time records. The Judge agreed. However, the witness evidence set out the basis for the hours claimed. This was an estimate of time spent dealing with the ETE System problems, based on payroll salaries. In cross-examination of the relevant witness, the witness explained that his approach had been conservative. The Judge, who of course saw the cross-examination, accepted this saying that there was no material before him upon which he could conclude that the sum claimed was unreasonable. Thus this case provides an interesting example of the value of careful witness evidence being used to support claims in respect of costs where there was a lack of written documentation.

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.
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Edited by Jeremy Glover, Partner, Fenwick Elliott LLP
jglover@fenwickelliott.com : Tel: + 44 (0) 207 421 1986

Fenwick Elliott LLP
Aldwych House
71-91 Aldwych
London WC2B 4HN
www.fenwickelliott.com