

CONSIDER THIS

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Material Breach: The Material Cases

In a difficult market, termination clauses assume a greater significance than ever. Faced with the possibility of escaping from an uneconomic project, a client may look to the contract for a weapon that will give him a legitimate excuse to terminate it. Often he will reach for a "material breach" clause.

In law, a party can treat a contract as discharged for repudiatory breach. That includes breach of a condition (a term that goes to the root of the contract), or potentially breach of an innominate term if the breach is serious enough. The innocent party has a choice. He can elect to treat the contract as discharged: in effect, to terminate. Alternatively he can hold the other party to it. In either case, the party in breach remains liable to pay damages, to the extent that there are losses within the scope of the law on remoteness of damage.

There are many variations on the theme of material breach clauses. In contracts for the building of ships or drilling units, it may appear as an instance of "Builder's default". Assuming that the right of termination is expressed to apply only to material breach, or breach of a material obligation, what sort of breach will trigger it? There is a series of recent cases in which the English court has considered clauses of this sort. These include Gallaher International Ltd v Tlais Enterprises Ltd. Mr Justice Christopher Clarke said:

"Materiality has to be assessed in the context in which the question arises which, here, is the possible termination of a five year agreement. In order for a breach to be material it does not have to be repudiatory ... In Phoenix Media Ltd v Cobweb Information ... Neuberger J, as he then was, said: 'Materiality involves considering the following: the actual breaches, the consequence of the breaches to [the innocent party]; [the guilty party's] explanation for the breaches; the breaches in the context of [the contract]; the consequences of holding [the contract] determined and the consequences of holding [the contract] continues.' I respectfully regard that as a helpful check list."

In Crosstown Music Company v Rive Droite Music Ltd, Crosstown took an assignment of copyrights - owned at the time by Rive Droite ("RD") - in songs written by two individuals ("the Writers"). The relevant term was as follows:

"In the event that the Publisher shall be in material breach of the terms of this Agreement and shall fail to take all reasonable action to remedy such breach within 45 days of written notification in reasonable detail of such breach from the Writer all rights assigned to the Publisher hereunder shall forthwith revert to the Writer."

Mr Justice Mann said:

"... [M]ateriality in the agreement before me ... does not mean that the breach has to be, or has to be close to, repudiatory. I also do not think it necessary or appropriate to require that the breach be vested with the character of going to the root of the contract. That is close to the notion of repudiation, and the concept of 'materiality' in my view stops short of that. The word 'material' certainly excludes that which is trivial, but beyond that it is appropriate to measure materiality by reference to the sort of considerations referred to by Neuberger J. If it be said that the clause, which admittedly has potentially very serious effects if triggered, is capable of giving rise to unfairly harsh consequences in respect of breaches that might not be very serious, so that some particularly stringent meaning must be given to the word, then the answer lies in considering the mechanism of the clause. It does not operate automatically on any 'material' breach. It only operates once a 'material' breach has been identified as such by the Writers and then goes unremedied by RD. Why should the Writers not have the right to have their copyrights back if a breach of significance is identified and the Publisher does not remedy it? In the context of an agreement such as the agreements in this case, that seems to me to be a fair and commercially sensible position and to be well within the contemplation of both parties. Accordingly, I do not think it necessary to give the word 'material' the forceful meaning contended for It connotes the concept of significance, as opposed to triviality, and its materiality has to be measured in its total context."

In some circumstances, it might be possible to argue that the express right of termination applies only to breaches that are of a continuing nature and that are capable of remedy, leaving the Company to rely on its common law rights for repudiatory breach in all other situations (National Power plc v United Gas Company Ltd).

But it is uncertain in each case how a court or arbitrator will interpret the words "material breach" or "breach of a material term". Not only will the interpretation always depend on its context in the contract as a whole but, as the law stands, it will be relevant to apply the "check list" of which the judge approved in Gallaher. What is clear is that in recent cases the word "material" has not been construed as synonymous with "repudiatory". Even a clause which allows the contractor a certain time to remedy the breach can be stringent. While the court or tribunal should take account of the seriousness of the commercial consequences for the parties, it might regard an opportunity to remedy the breach as a factor militating in favour of a broad interpretation of the word: it may be inclined to read the word "material" as applying to everything other than minor breaches if this does not result automatically in a termination. In practice, that opportunity may give a contractor very little cause for comfort.



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A brief review of commercial issues relevant to the construction, engineering and energy industries.

Delay Analysis Techniques Available For Project Managers In Construction Contracts

By Bob Breeze, Group Managing Director
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There has been much written about the contentious subject of delay analysis in construction contracts and I am hesitant to add to the subject. However, most of the case law and text books are based in the onshore construction world (building and civil engineering mainly) where standard forms of contract are usually employed whether that be from the JCT, ICE or NEC stable.

In the UK the Society of Construction Law has published many a valuable article including several on delay analysis and there are several text books on the subject yet we still see the same old issues arising time and time again in construction contract delay claims – why is that?

The most important thing to remember in any delay analysis situation is that it is no good simply regurgitating the doctrines as espoused in a popular text book or recent article from a published journal or Society. The facts must always be set in the framework of the particular contract which regulates the relationship between the relevant parties.

It is also important to remember that the often quoted saying "time is money" does not apply to delay analysis. Simply proving an entitlement to an extension of time does not of itself give rise to an entitlement for a payment for additional prolongation costs. It merely relieves one party from the liability for liquidated damages for failure to complete on time.

In many construction contracts a delaying event which gives rise to an entitlement for an extension to the date for completion is often referred to as "Permissible Delay". For present purposes I will refer to a delaying event which does not give rise to an entitlement to an extension of time as "Culpable Delay".

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Stapleton is a long established firm of consultants investigating contractual, financial and management issues within the construction, engineering and energy industries.

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The first consideration is whether or not the contract sets out any administration requirements for the provision of a programme (or schedule as it is more often referred), to and regular reports as to progress in comparison to the schedule and periodical updates of the schedule. The better drafted construction contracts usually have such requirements set out in an appendix to the terms and conditions of contract. Even better, set out these requirements in the invitations to tender.

The very first step in demonstrating a Permissible Delay has occurred is to show what the planned intention was for how the work was to be executed. This is often called the Contract Master Schedule. This normally includes a schedule, "S" curves, manpower histograms and a list of key client and contractor deliverables and may be based on a method statement of build sequence.

The next step is to ensure that any contractual notification requirements have been satisfied as it is often a requirement that any delay, Permissible or otherwise, has to be notified even if it is only "likely" to occur. That is to say you have to be constantly on the lookout for all delays past, present or future and those that are Permissible Delays may only give rise to an entitlement to an extension of time if the required notices have been issued in a timely manner. That way all mitigation measures will have been given time to be implemented such as the cancelling of an order for extra works if it is likely to cause delay or the introduction of acceleration measures.

Assuming those two initial steps have been satisfactorily achieved, we then need to move into the murky waters of how to make an assessment of such events and their impact on the date for completion in the contract.

Many construction contracts are drafted with wording along the lines of only "demonstrable delay" or "verifiable delay" will give rise to an extension to the completion date, others may use terms such as "such delay as is reasonable". In either case it is incumbent upon the claiming party to demonstrate either what

as a fact has happened or to show what was reasonable in all the circumstances. This usually involves the preparation of a retrospective comparison of the As-Built events in comparison to the Contract Master Schedule which should be updated to take account of actual progress to the point of a delaying event occurring. It is also necessary to show that the schedule for the remaining work could in fact have been achieved before it can be used in any comparison to the actual As-Built scenario.

It is then necessary to show what were the critical activities as it is only delay to these events which will cause delay to completion. Delay to non-critical activities can of course still give rise to a claim for additional cost but not an extension of time unless of course the delay is so prolonged that this activity then becomes critical.

The reality is that the critical path moves throughout the life of a project and other issues such as float and concurrent delays creep in to the frame. So how do we deal with these?

The three main questions which arise in almost every delay analysis situation are:

1. What method should be used to analyse delay to a project;
2. What is the effect of concurrent delays on entitlement to an extension of time;
3. Who owns the float in the schedule?

There are several competing theories as to how delay analysis should be carried out but none of them are perfect and the selection of a method is often dependent upon the quality and quantity of the available historical information. In fact, in the UK today there is still no precedent which clearly spells out the way in which the Courts believe it should be done. There are a number of conflicting alternatives such as the theoretical approaches of the "As-Planned Impacted" and the "As-Built But For" methods and the more factual approaches such as the "As Planned versus As-Built" or the "Windows or Snap-Shot" methods. There are others but I do not intend to compare all of these alternatives here but to give a view as to the current situation as I

understand it to be.

The first two of the above questions were addressed in the recent Scottish case of *City Inn Ltd -v- Shepherd Construction Ltd* [2008] BLR 269. The judge recited the history of delay cases and made a thorough review of the evidence in the case before him and had to come to a decision as to the best method to adopt where there were competing delaying events which occurred concurrently. He concluded that it was reasonable to apportion delay between Permissible Delay and Culpable Delay and that a fair and reasonable extension of time can be granted on that basis.

What is of greater interest is that he went on to say:

"...it may be possible to show that either a [Permissible Delay] or a [Culpable Delay] is the dominant cause of that delay, and in such a case that event should be treated as the cause of the delay"

The point of interest is his selection of the "Dominant Cause" approach which was expressly condemned by the judge in the English case of *H Fairweather v London Borough of Wandsworth* (1987) 39 BLR 106. Other legal commentators have expressed the view that the English Courts are unlikely to adopt the Dominant Cause approach and would not overrule the *Fairweather* case. This is because the English Courts are not bound to follow a Scottish court decision although they are persuasive and are often followed. There is however, a risk that an Adjudicator or Expert appointed to decide such matters may still follow the *City Inn Ltd* precedent in the absence of any clarification from the English Courts.

The current situation in dealing with concurrent delaying events in any delay analysis within English Law jurisdictions remains as set out in the case of *Henry Boot Construction (UK) Ltd v Malmaison Hotel (Manchester) Ltd* (1999) 70Con LR32, TCC. Where there are two concurrent causes of delay, one of which is Permissible Delay and the other is not, then the claimant is entitled to an extension of time for the period of delay caused by the Permissible Delay.

So for example, if it is impossible to do any work on a site due to a Permissible Delay of lets say exceptionally inclement weather but at the same time the contractor does not have any labour available which is not a Permissible Delay, then the contractor is entitled to an extension of time despite the fact that a delay would have occurred in any event by reason of the lack of labour.

Of course it remains to be proven in any given case that a Permissible Delay did in fact cause a delay to completion of the works and that any other delaying events were also proven factually before the above delay analysis can be applied.

Finally, the situation where a Permissible Delay event occurs during a period of overrun after the date for completion has passed and for which delay the contractor is culpable, was cleared up in the case of *Balfour Beatty Building Ltd v Chestermount Properties Ltd* 62 BLR 1 QBD. The contractor is entitled to the nett effect of any such delay to be "dotted on" to the end of the contract period even though that new date for completion may have already passed.

That only leaves the third question of who owns the float?

It may be helpful to first of all describe what is meant by "float" or "slack" in a construction schedule. It can be defined as the amount of time between the early start date and the late start date or the early finish date and the late finish date of any of the activities in the program. So it can be either at the start or end of an activity (called Activity or Free Float) or it can be from the latest end date of the last activity to the date for completion in the contract (called Total Float). Of course activities on the critical path have no float so that any delay to that activity will lead to a delay in completion of the works, unless acceleration measures are introduced e.g. extra resources, extra shifts, subcontracting etc.

Some contracts make provision for the ownership of float so that for instance, if a contractor's program shows Total Float and that is eroded by an act or omission of the employer, then he may have a contractual right to retain that float by being granted

an extension of time even though the delay would not take him past the contractual date for completion. That is seen as being fair as it maintains the risk allowance built into the tender and hence contract by the contractor. He is still exposed to risk of delays so he should not lose that allowance by virtue of the employer's interference.

However, that provision is rarely included in many contracts and the situation is often taken as being whoever gets to the float first is entitled to use it. In other words, the employer can delay the progress of the work and not have to extend the date for completion as the Total Float may be adequate to accommodate any such delay.

In English Law it is still very much an unresolved question of who owns the float. Every case has to be examined on its facts and contractual obligations and it is often a matter of common sense as to who can use the float which often boils down to a chronological analysis of events and their effect on completion.

In summary therefore it seems to me that there are no hard and fast rules set down by the English Courts as to how to go about delay analysis. It is essential to consider all of the evidence which will include witness testimony, documentary evidence such as photographs, progress reports, variations, change orders etc as well as expert opinion which may include a delay analysis exercise. This has then to be considered in light of the contractual rights and obligations as well as established precedent. However, the Courts have shown their intolerance recently for self appointed delay experts who make the exercise far more complicated than it need be and also lose sight of the facts of the case which is often linked to the use of complicated computer software programs upon which they rely for their answers. They do so at their own peril!

