Fenwick Elliott
Solicitors

Dispatch

Issue 96
June 2008

Dispatch highlights a selection of the important legal developments during the last month.

Letters of Intent

■ **RTS Flexible Systems Ltd v Molkerei Alois Müller GMBH & Co KG (UK Productions)**

As Mr Justice Clarke said, this case is another example of the "*perils of proceeding with work under a letter of intent*". RTS provided quotations to design, manufacture, assemble, install and commission automated equipment to package yoghurt pots. Once Müller had decided to award the contract to RTS, a letter of intent was sent out. The letter of intent anticipated that the full terms and conditions would be agreed and signed within four weeks of the date of the letter. Those terms would be based on the MF/1 Contract. It was also noted that "*prior to agreement on the full contractual terms, only Müller shall have the right to terminate this supply project and contract*". If Müller exercised the right to terminate, it would reimburse RTS' reasonable out-of-pocket expenses. No final agreed form of contract was agreed and/or executed.

The Judge, having analysed the communications between the parties, determined that the following had occurred. RTS had submitted a quotation to carry out certain works based upon their own standard terms. The letter of intent issued by Müller was a counter offer which was accepted by RTS in writing subject to two qualifications, one of which was that the equipment would be commissioned by a particular date.

In the view of the Judge, the language of the letter of intent made it clear that the parties were agreed that they had entered into a contract of some sort pursuant to that letter of intent. The problem was that although the parties had contemplated agreeing final terms within four weeks, they did not clearly express what was to be the position if, as turned out to be the case, they failed to do so. The Judge regarded it as being implicit in the agreement that upon the expiry of the four weeks, the letter of intent agreement would come to an end.

Müller's wish to proceed was subject to the full contractual terms and relevant technical specifications having been finalised, agreed and signed within that timescale. The letter of intent gave Müller a right to cancel upon payment only of expenses and cancellation costs. This was entirely reasonable during the four week period but wholly inappropriate for the entire duration of the project.

Therefore, the Court then had to consider the contractual position after the expiry of the letter of intent. RTS had continued to build and deliver the equipment and they were partially paid for it. In these circumstances, the Judge noted that a Court will usually infer that the parties have entered into some contract even if it cannot be precisely spelt out. It appeared to the Judge that after the lapse of the letter of intent, the parties had reached an agreement on the work that was to be done for a price they had already agreed. It was not essential for the parties to agree the terms and conditions beyond that and they did not do so. They simply carried on as before, calling for and carrying out work without agreement as to terms. However it was unrealistic to suppose that they had not intended to create some form of legal relationship between them.

RTS suggested that the contract included the standard MF/1 conditions. The Judge was not prepared to infer that the parties' contract did this. For example, the letter of intent indicated that the final terms were not to be contractually agreed until signature. Also, the parties did not proceed on the basis of the MF/1 conditions. For example, RTS did not procure the provision of an advanced payment guarantee which under the MF/1 conditions was required prior to the advance payment being made. Further, Müller did not appoint an engineer and the dispute procedure was not followed.

Müller's primary obligation was to pay RTS the agreed lump sum in return for the goods and service to be provided by RTS. The parties agreed on the work that was to be done, including a test and build schedule, and the total price. They also agreed on the stage payments that were in fact made. However, they made no further binding agreement as to when the remaining 30% would be paid. There were discussions but no agreement was reached. In these circumstances, the Judge held that the general rule for lump sum contracts should apply. Müller was therefore bound to pay (subject to set off) the balance of the contract price upon substantial completion of the work. Substantial completion would occur once the site acceptance tests had been passed.

In respect of any additional work requested by Müller outside the scope of the contract, RTS was entitled to be paid a reasonable sum for such work. An implied contract came into being as a consequence of Müller requesting such work and RTS complying with that request in circumstances where it was plainly not acting for free.

Framework Agreements

■ **Henry Brothers (Magherafelt) Ltd & Ors v Department of Education for Northern Ireland**

The claimants sought an injunction restraining the Education Department from concluding a framework agreement for the modernisation of schools in NI. The specific projects were to be based on the NEC3 form of contract. The contractors, who were to be assessed according to their direct fee percentage, suggested that the assessment criteria was neither rational nor lawful.

The Department's view was that as all the contractors would be sourcing their material and labour force from the same market, the basic costs of the work would not greatly vary between them. The tender documents had explained that the NEC3 contracts contained two financial elements, namely the defined costs calculated by reference to the schedules of costs components and the fee percentage. The Department did not seek actual costs at this stage and felt that such a calculation would not have been possible since the vast majority of projects had not yet been identified or designed. Further, final accounts for construction schemes typically bore little resemblance to the tender prices. Thus the only real objective commercial assessment was the application of the percentage fees.

Under the EU procurement regulations, a contracting authority shall award a public contract on the basis of the offer which is either most economic and advantageous from the point of view of the contracting authority or the lowest price. Equal treatment implies an obligation of transparency in order to enable compliance to be verified and thus the award criteria must be formulated in the tender documents in such a way as to allow each and every reasonably well-informed and diligent tenderer to interpret it the same way.

The claimants said that to rely upon the fee percentage as the determinative commercial criteria to the exclusion of any other objectively verifiable element of cost was manifestly wrong. Costs would significantly vary between contractors. Efficiency levels vary and particular contractors would be able to negotiate different rates for labour and materials. It might be possible for one contractor to offer a lower overall price than another even though it was charging a higher percentage fee. A more accurate comparison of the relative commercial bids could be gained by requiring bidders to price a sample project.

Coglin J was satisfied that there was a serious question to be tried here. There was a need to ensure the public funds were spent honestly and efficiently on the basis of a genuine tender assessment. Equally, it was possible to argue that the use of the percentage fee as a pricing mechanism was a transparent and objective criteria aimed at identifying the most economically advantageous tender. However, the public had a strong interest in ensuring that refurbishment of the schools estate took place as speedily and efficiently as practicable. Ultimately, therefore, whilst the Judge agreed that the questions raised by the claimants needed to be authoritatively determined, he was not prepared to grant or issue an injunction at this stage.

Settlement - Offers and Counter-Offers

■ **Cantor Index Ltd v Thompson**

After Cantor had raised a claim against Thompson, the following occurred:

(i) On 22 February, Thompson made a settlement offer offering payment in instalments, with the first payment being made on 1 March;
(ii) On 23 February, Cantor made a counter-offer;
(iii) On 1 March, Thompson repeated the original offer and enclosed a cheque by way of the first payment;
(iv) On 2 March, Cantor received a cheque from Thompson, which was paid into its bank account;
(v) On 5 March Thompson advised that there was a problem with the cheque; Cantor in return advised that it had been cashed. However on the same day, Cantor learnt that the cheque had been returned unpaid;
(vi) On 9 March, Cantor then wrote to Thompson demanding payment of the first instalment by 14 March, otherwise it would proceed to take legal action as set out in its letter of 23 February 2008.

Tugendhat J had to decide whose offer had been accepted and when. Thompson said that the reference in the 9 March letter to the 23 February offer, meant that Cantor had not accepted the offer of 1 March. Cantor said that reference was a statement of subjective belief as to the agreement thought to have been made. Cantor now accepted that that belief was mistaken and argued that by its conduct in immediately presenting the cheque for payment, it had accepted the terms of the offer made in the 1 March letter. Accordingly a binding agreement was reached. The Judge agreed. The key was the payment in of the cheque. This represented objective evidence of acceptance of the 1 March offer by conduct. The cashing of a cheque is always treated by the courts as being strong evidence of the acceptance of an offer.

Dispatch **is produced monthly by Fenwick Elliott LLP, the leading construction law firm which specialises in the building, engineering, transport, water and energy sectors. The firm advises domestic and international clients on both contentious and non-contentious legal issues.**
Dispatch **is a newsletter and does not provide legal advice.**

Fenwick Elliott
Solicitors

Aldwych House
71-91 Aldwych
London WC2B 4HN

T +44 (0)20 7421 1986
F +44 (0)20 7421 1987
Editor Jeremy Glover
jglover@fenwickelliott.co.uk
www.fenwickelliott.co.uk