FIRST DIVISION, INNER HOUSE, COURT OF SESSION

[2021] CSIH 50
CA143/19

Lord President
Lord Menzies
Lord Woolman

OPINION OF THE COURT

delivered by LORD WOOLMAN

in the reclaiming motion by

VAN OORD UK LTD

Pursuers and Reclaimers

against

DRAGADOS UK LTD

Defenders and Respondents

Pursuers and Reclaimers: Moynhian QC; Burness Paull LLP
Defenders and Respondents: Walker QC; CMS Cameron McKenna Nabarro Olswang LLP

5 October 2021

Introduction

[1] In 2016 Aberdeen Harbour Board embarked on the construction of a new harbour at Nigg Bay. It employed Dragados as the main contractor on this major expansion project. In turn Dragados engaged Van Oord UK Ltd as the dredging subcontractor.

[2] The terms of both the main contract (20 December 2016) and the subcontract (16 March 2018) were based on the third revision of the New Engineering Contract ("NEC3").

[3] During the course of the subcontract, Dragados transferred about one third of the dredging to two other companies. Later it informed Van Oord that it proposed to reduce the sum payable for Van Oord's remaining work under the "compensation event" provisions of NEC3.

[4] The proposed reduction was a significant one. The bill of quantities specified £7.48 per cubic metre (m^3) as the rate for dredging. Dragados proposed to reduce it, in June 2019, to £5.82m^3, a 22% reduction, and further in September 2019 to £3.80m^3, a 49.2% reduction.

[5] Van Oord contested the reduction on the basis it was invalid, as Dragados had breached the subcontract. It sought payment at the original bill rate.

[6] The commercial judge heard a debate at first instance. He held that the transfer of work by Dragados constituted a breach of the subcontract. He also concluded, however, that Dragados was entitled to reduce the bill rate payable to Van Oord for the remaining works. His decision largely mirrored the outcome of earlier adjudications, which had found in favour of Dragados.

[7] Breach is now accepted. So the question for determination is this. Was Dragados entitled to reduce the sums payable to Van Oord? The answer turns on the proper construction of NEC3.

Background

[8] Van Oord undertook to dredge an estimated 2,150,000m^3 of material to create the

new harbour. It also agreed to carry out various other works, including caisson filling. The total value of the subcontract was about £26.4m.

[9] In its tender Van Oord inserted a 'blended' rate for the dredging. That rate averaged out the cost of easier and more difficult works. Van Oord selected the rate on the footing that it would undertake all the dredging work.

[10] Van Oord began dredging on 5 May 2018. Within a short period, Dragados began issuing notices to omit certain dredging, which it transferred under the following contractual arrangements:

Date (2018)	*Company*	*Volume*
15 May	WASA Dredging UK Ltd	400,000m^3
14 December	Canlemar SL	300,000m^3

The formal subcontract with Canlemar was preceded by a letter of intent dated 13 August 2018.

[11] Van Oord did not learn about the transfers for some time. It raised this action in September 2019. At that stage it sought various orders, including *interim* interdict against further transfers of dredging work. Its application was unsuccessful. The commercial judge concluded that the balance of convenience tipped in favour of Dragados, because it had entered into binding obligations with WASA and Canlemar.

[12] Dragados terminated the subcontract on 6 March 2020. The issue now concerns the correct valuation of the dredging works in the termination account. Van Oord seeks (i) declarator that Dragados was not entitled to reduce the sum payable to it for work done consequent upon the disputed instructions, and (ii) payment of a sum based on the original bill rate.

[13] The parties advance various claims and counterclaims. Some of the disputes can only be resolved by means of evidence.

[14] The theme of unfairness underpins Van Oord's position. It contends that Dragados is seeking to manipulate the contract in its favour. Had Van Oord known that it would be left with a disproportionately higher share of the more difficult work, it would have increased the dredging bill rate in its tender. Van Oord claims that Dragados: (a) insisted on a blended rate in the tender; (b) transferred more of the easier work to the other two companies; and (c) did so to avoid having to pay standby charges (at least in the case of WASA).

[15] Dragados argues that there has been no manipulation on its part. It maintains that NEC[3] provides a blueprint for the circumstances that have arisen. It also maintains that the recalculation yields a fair result to Van Oord, which would otherwise receive a windfall benefit. With regard to factual matters, Dragados claims that Van Oord: (a) showed poor productivity; (b) would have made a loss on the transferred work; (c) facilitated the transfer of works to WASA; and (d) would be left neither better nor worse off by the NEC[3] compensation event mechanisms.

NEC[3]

[16] Like all standard form contracts, NEC[3] consists of a series of interlocking terms.

Relevant Terms

[17] The following clauses are at the centre of the dispute:

Clause 10.1:

> "The Contractor and the Subcontractor shall act as stated in this subcontract and in a spirit of mutual trust and co-operation."

Clause 14.3:

> "The Contractor may give an instruction to the Subcontractor which changes the Subcontract Works Information or a Key Date. The Contractor may, in the event that a corresponding instruction is issued by the Project Manager under clause 14.3 of the Main Contract only, also give an instruction to omit a) any Provisional Sum and/or b) any other work, even if it is intended that such work will be executed by Others. The Subcontractor has no claim for loss of revenue, loss of opportunity, loss of any contract, loss of profit or for any indirect loss or damage against the Contractor in relation thereto."

Clause 27.3:

> "The Subcontractor obeys an instruction which is in accordance with this subcontract and is given to him by the Contractor."

Clause 60.1:

> "The following are compensation events … (18) A breach of subcontract by the Contractor which is not one of the other compensation events in this subcontract or any act of prevention."

Clause 60.4:

> "A difference between the final total quantity of work done and the quantity stated for an item in the Bill of Quantities is a compensation event if
>
> - the difference does not result from a change to the Subcontract Works Information,
> - the difference causes the Defined Cost per unit of quantity to change and
> - the rate in the Bill of Quantities of the item multiplied by the final total quantity of work done is more than 0.5% of the total of the Prices at the Subcontract Date.
>
> If the Defined Cost per unit of quantity is reduced, the affected rate is reduced."

Clause 60.6:

> "The Contractor corrects mistakes in the Bill of Quantities which are departures from the rules for item descriptions and for division of the work into items in the method of measurement or are due to ambiguities or inconsistencies. Each such correction is a compensation event which may lead to reduced Prices."

Clause 63.2:

> "If the effect of a compensation event is to reduce the total Defined Cost, the Prices are not reduced except as stated in this subcontract."

Clause 63.4:

> "The rights of the Subcontractor to changes to the Prices and the Subcontract Completion Date are its only rights in respect of a compensation event."

Clause 63.10:

> "If the effect of a compensation event is to reduce the total Defined Cost and the event is
>
> - a change to the Subcontract Works Information or
> - a correction of an assumption stated by the Contractor for assessing an earlier compensation event,
>
> the Prices are reduced."

Did Dragados act in good faith?

[18] Clause 10.1 provides a useful starting point. The commercial judge concluded that this term did not add much. He instead based his decision on the cluster of clauses that regulate compensation events. Mr Walker invited us to take the same approach.

[19] We decline to do so. In our view clause 10.1 is not merely an avowal of aspiration. Instead it reflects and reinforces the general principle of good faith in contract: McBryde, *The Law of Contract in Scotland* 3rd edition paras 17-23 to 17-34.

[20] In particular, clause 10.1 aligns with three specific propositions:

(i). A contracting party "will not in normal circumstances be entitled to take advantage of his own breach as against the other party": *Alghussein Establishment* v *Eton College* [1988] 1 WLR 587, 591D-E, per Lord Jauncey.

(ii). A subcontractor is not obliged to obey an instruction issued in breach of contract: *Thorn v The Mayor and Commonalty of London* (1876) 1 App. Cas. 120, per Lord Cairns (LC) at 127-128.

(iii). Clear language is required to place one contracting party completely at the mercy of the other: *Parkinson (Sir Lindsay) & Co. Ltd v Commissioners of His Majesty's Works and Public Buildings* [1949] 2 KB 632, 662 per Asquith LJ.

[21] Mr Moynihan places special emphasis on the first proposition, although accepting that he did not cite it to the commercial judge.

[22] Lord Jauncey's statement embodies the doctrine of mutuality. A party cannot enforce a contractual stipulation in its favour, if it is the counterpart of another obligation which it has breached: see *Macari* v *Celtic Football and Athletic Co Ltd* 1999 SC 628 at 640G-641D, per the Lord President (Rodger), and *Bank of East Asia* v *Scottish Enterprise* 1997 SLT 1213, per Lord Jauncey at 1216L-1217K.

[23] We conclude that clauses 10.1 and 63.10 are counterparts. Unless Dragados fulfils its duty to act "in a spirit of mutual trust and co-operation", it cannot seek a reduction in the Prices. Accordingly, Van Oord has pled a relevant case to go to proof. Evidence can be led to evaluate Dragados' conduct. Did it act in a spirit of mutual trust and co-operation? Or did it act in a contrary manner?

Did the instructions lead to a reduction in the dredging rate?

[24] Each breach by Dragados constituted a compensation event. That is because of the "catch all" wording of clause 60.1(18).

[25] NEC[3] contains a complex formula to assess the value of a compensation event. Happily it is not necessary to carry out the exercise here. The parties agree that there is a

reduction in the Defined Cost. They disagree, however, on whether there is also a reduction in the Prices and the bill rate payable for the remaining work.

[26] By way of clearing the ground, breach of contract is not such an occasion (clauses 60.4, 60.6 and 63.10). Accordingly, the breach of contract by Dragados does not give rise to a reduction in the Prices, even if its effect is to reduce the total Defined Cost.

[27] The commercial judge held that clause 63.10 governed the situation. He held that the sole remedy available to Van Oord was to have that change assessed in accordance with the compensation event pricing mechanism (clause 63.4).

[28] Mr Walker urged us to accept that approach, which he amplified as follows. Recalculation arises because of Van Oord's pricing strategy and its failure to achieve its productivity rates. It would have made a loss if it had completed the omitted work. Payment at the original bill rate would result in it receiving a windfall benefit. The aim of the recalculation is to place both parties in the same position as they would have been in if the breach had not occurred. Neither would be better or worse off. So Dragados gains no advantage by this procedure.

[29] We reject that argument. NEC[3] states that all compensation events are *valued* in the same way (clause 63.1), but continues that if

> "the effect of a compensation event is to reduce the total Defined Cost, the Prices are not reduced except as stated in this subcontract" (clause 63.2).

We conclude that, properly construed, clause 63.10 applies only to a *lawful* change. It excludes instructions issued in breach of contract. They are invalid, because they are not given "in accordance with this subcontract" (see clauses 14.3 and 27.3). The natural synonym for "in accordance with" is "consistent with". A breach is plainly inconsistent with the contract.

[30] We add these points in support of our interpretation. First, it means that all breaches are treated equally. None produces a reduction in the Prices. Second, it avoids the suggestion that Van Oord was bound to obey a "breach instruction". That cannot be right. To take a fanciful example, it would have been under no obligation to build a hotel if Dragados had issued such an instruction. Third, the NEC[3] should not be charter for contract breaking.

Conclusion

[31] We shall recall the interlocutors of the commercial judge dated 7 October 2020, and allow a proof before answer. We shall sustain Van Oord's second plea in law to the extent of excluding from probation those averments in Answers 14, 15 and 20 stating that Dragados is allowed to reduce the bill rate.