JUDGMENT : His Honour Judge Humphrey LLoyd QC. QBD, Official Referees' Business. 29th February 1996

1. This action arises out of a written contract made in 1990 between the plaintiff (Foster Wheeler) and the defendant (Chevron) whereby Foster Wheeler undertook engineering and other obligations.

2. Chevron is the operator of Ninian Southern and Ninian Central which are oil platforms in the Ninian field (lying within North Sea Blocks 3/3 and 3/8). As set out in the defence, in about 1989 because oil production had declined and with it field gas, both the platforms had spare capacity for processing oil and gas. Accordingly Chevron, together with the other companies which participate in the Ninian Group, decided that it would have the platforms modified so that they could receive and process fluids from nearby fields (Lyell, Staffa and Strathspey). Production of the platforms was to be maintained during the project. The Ninian Southern platform was to be adapted to receive and process oil and gas from the Lyell and Staffa fields and to produce water injection for Lyell and Strathspey. The Ninian Central platform was to be adapted to accommodate facilities to receive and process oil and gas from the Strathspey field. As a result of the modifications the equipment and services on the platforms would thereby come to be used by third parties.

3. Foster Wheeler were engaged to design the modifications to the existing facilities and the installation of additional facilities to allow the use of the platform by the third party entrants. The contract was aptly described as "incremental" as it envisaged that there would be three successive phases:

4. The price payable by Chevron to Foster Wheeler was dependent upon agreement of the CTRs since the contract was one described as for *"reimbursable costs"*. In this instance the term did not mean that the contract was of a *"cost-plus"* nature but that rates would be agreed for the personnel involved and payment would be made for the hours worked by them as set out in the CTRs whereby Foster Wheeler would be reimbursed their "costs", as defined by the contract Exhibits. The contract provided for invoices to be submitted to and paid by Chevron.

5. Foster Wheeler duly submitted invoices but some were not paid. The invoices included claims under six heads: reprographics; affiliates; re-working; quality assurance/control; agency fees; and Mentor Project Engineering Ltd. As a result of Chevron's non payment Foster Wheeler issued a writ on 28 December 1994 for invoices submitted between September 1993 and June 1994. The defence was served on 24 April 1995.

6. Chevron's defence is in part that it has been overcharged in that Foster Wheeler have used the wrong bases for its invoices, but, for present purposes, the most important issue concerns claims in respect of allegedly defective designs which affects invoices classified as "re-working". Chevron's case is that Foster Wheeler made many errors in the preparation of the designs and drawings and other documents as a result of which Chevron has incurred costs and suffered loss and damage amounting to many hundreds of thousands of pounds. In paragraphs 49 - 56 of its defence Chevron maintain that Foster Wheeler were in breach of clauses 2.2(d), 3.1.2(c), 3.3.2(c), 3.3.3[1] and 3.4 of the contract conditions. Chevron also contend that it was entitled to set off in extinction or diminution of Foster Wheeler's claims the overpayments made to Foster Wheeler and the loss or damage which it has suffered (which is also the subject of a counterclaim).

7. In paragraph 11 of the defence, Chevron plead that it was an implied term of the contract that: *"If and to the extent that the defendant was required to reimburse the plaintiff for hours worked, costs incurred and/or the services provided at the rates and prices contained in the Exhibit II, the defendant was only obliged to pay for hours worked, costs incurred and/or services which had been reasonably and properly incurred and/or provided for."*

   Accordingly part of Chevron's case was that the sums claimed in the invoices included amounts which had not been reasonably and properly incurred by Foster Wheeler (as well as in accordance with the contract). In the event it seems that the Phases did not proceed exactly as originally contemplated and the terms of the contract were varied by a number of variations of which Variation 02 and Variation 14 are considered relevant. Variation 02 was both an instruction to proceed with Phase II (Detailed Engineering Work) and an alteration of the original labour rates.

8. Foster Wheeler's case is that Phase I was accepted on 12 November 1992 and Phase 2 was accepted on 29 June 1993. Accordingly, Foster Wheeler say that Chevron's claims relate to errors in its work discovered prior to the Acceptance of Phase 2. These dates are not admitted by Chevron and for present purposes it is necessary to consider the case on the assumption that errors may have been discovered after Completion and Acceptance of a Phase or a Segment, since each Phase might be split into a number of Segments.

9. This distinction is material to Foster Wheeler's case since in its reply and defence to the counterclaim Foster Wheeler maintain that the contract limited its liability for the design errors relied upon by Chevron, and in argument drew attention to the position before and after Acceptance.

10. Since claim, defence and counterclaim all raised a formidable number of issues of fact many of which might not have to be decided were some of the principal arguments of law to be resolved in favour of the party proposing them, a trial of preliminary issues was ordered. The issues were subsequently agreed as follows:-

    1. (a) Whether the defendant has any right at common law to set off damages sustained by it as a consequence of breaches of contract on the part of the plaintiff. (b) Whether the defence of abatement is excluded by the contract. 2. Whether it was an implied term of the contract that reimbursable costs would be reasonably and properly incurred. 3. Whether the plaintiff's liability for defects in design was limited in the manner alleged by the plaintiff in paragraph 50A of the Amended Reply and Defence to Counterclaim.

[1] No clause 3.3.3 exists and this must refer to 3.3.4

For completeness it is necessary to set out the text of paragraph 50A referred to in Issue 3:-

"50. The alleged breaches at paragraph 50 of the Defence are denied. The plaintiff may plead further to the Schedules to be served in support. Without prejudice to the forgoing denial the plaintiff avers as follows:

A: To the extent, which is denied, the defendant establishes any breach against the plaintiff, the liability of the plaintiff is limited as follows:

Post Acceptance

(i) The extent of the plaintiff's liability under Section 3 is limited to:
(a) correcting such Designs as are covered by the Guarantee and
(b) correcting any portion of the Facility damaged by the defect or its repair.
(c) in the alternative to (a) and (b), payment of the actual direct cost of corrective work performed by others.

(ii) It is expressly denied, if the same be alleged, that such liability extends to the plaintiff reimbursing the defendant for any cost or expense allegedly incurred, whether during the performance of the Contract or otherwise.

(iii Without prejudice to the forgoing, the Guarantee only applies after Acceptance as defined at Section 1.1(a) of the Contract and, in the premises, costs incurred or damage done by defective design during the currency of the Contract prior to acceptance are not subject to the Guarantee at all.

Prior to Acceptance

(iv) At sub-paragraph 10(viii) the plaintiff relies on Section 12 which expressly provides a procedure for the plaintiff to remedy defective work during the currency of the Contract and prior to Acceptance, which clause provides that the Guarantee is to be invoked by the defendant after Acceptance.

(v) The plaintiff further relies on Section 9.4 which expressly provides for the plaintiff's liabilities in respect of due care and diligence and the performance of the Contract. Such liability is expressly limited to "loss, damage or destruction of any property of the Group (including the Facility)". In the premises the plaintiff avers that it has no further liability beyond that provided by Section 9.4 which Section does not relate to the sums presently claimed.

(vi) Further, and to the extent as is necessary in relation to the particularised claim to be pleaded against the plaintiff, the plaintiff will rely upon Variation 14 dated 9 February 1993 which expressly provides that the plaintiff's obligations under, inter alia, Section 3.4 shall be limited to the replacement of any of the plaintiff's personnel who in the defendant's opinion is unsatisfactory and/or re-performance of their defective work at no cost to the defendant.

Without prejudice to A, and to the extent that the defendant contends that the plaintiff failed to perform its Works with due diligence and/or in accordance with generally accepted, current good practice of the industry and trades involved:

(vii) The plaintiff will contend that, on a true and proper construction, such a term as provided by Section 2.2 of the Contract specifies the standard against which the balance of the terms pleaded against the plaintiff at paragraph 50 of the Defence should be judged.

(viii) An "error-free" design would require such an extent of checking as to be uneconomical and that it is generally accepted and current good practice to accept that a certain amount of error will stay with the design to be identified and resolved on site as the most cost effective solution. This was particularly true under the Contract due to the uncertainty and under-estimation of the scope of the same as pleaded at paragraph 32 (ii) [of the Amended Reply and Defence to Counterclaim].

11. In opening Mr Colin Reese QC for Foster Wheeler stressed that the contract should be read as a whole and in sensible commercial terms. He relied upon a recent unreported decision of Mance J. (***Charter Reinsurance Co. Ltd v Fagan,*** 28 June 1995) but only for the extracts quoted by Mance J. from the judgments in the Court of Appeal in ***Arbuthnot v Fagan; Deeny v Gooda Walker Ltd,*** 30 July 1993, but also unreported). The section of the judgment of Mance J. upon which Mr Reese QC relied reads as follows:-

"The correct approach to construction

*The parties' submissions adopt different approaches to the issues of construction which arise. The Syndicates say that the words of the contracts alone are so clear that any further thought about their implications or aid to their true construction is not only unnecessary but wholly inappropriate; they cite words of Lord Halsbury in **Leader v Duffey** (1888) 13 App. Cas. 294 (a case concerning a marriage settlement) and **Smith v Cooke, Swinnerton** [1891] A.C. 297 (a case concerning a deed of assignment of a partnership business and property). Charter Re submit that construction should never be a wholly abstract or literal exercise, divorced from any consideration of context or practical implications.*

*On the one hand, the court should not approach the construction of any contract with notions of principle or reasonableness conceived in the abstract and seek to force the provisions of a particular contract into that straitjacket: cf per Saville J. in **Palm Shipping Inc. v. Kuwait Petroleum Corp. (The "Sea Queen")** [1988] l Lloyd's Rep 500, citing an earlier dictum of Lord Goff to like effect in **The "Notos"** [1987] 1 Lloyd's Rep. 503 at page 506.*

On the other hand, there is a wealth of authority, which is of particular relevance in the commercial context, that the court should seek to place itself in the same matrix as the parties were when contracting and to understand their general aim, objectively assessed, and that considerations of reasonableness or "commerciality" can play an important role in this exercise. Mr Kentridge cited passages from ***Antaios Co. Nav. S.A. v Salen Rederna A.B.*** *[1985] 1 A.C. 191, at pages 200E-201E and* ***F.L. Schuler A.G. v Wickman Machine Tool Sales Ltd.*** *[1974] AC 235, the familiarity of which in no way detracts from their forcefulness on re-reading in the present connection.*

For my part, I adopt and apply recent guidance given in the Court of Appeal in the unreported authority in ***Arbuthnot v Fagan: Deeny v Gooda Walker Ltd*** *(30 July 1993) where a similar issue about the correct approach to construction arose. The context was the wording of the standard form of agency agreement prescribed by Lloyd's byelaw prior to 1989; the language made it, according to the underwriting agencies, a condition precedent to the accrual of any cause of action against a particular agency in respect of a particular syndicate and year that the name must first pay all calls made upon him or her for underwriting expenses or liabilities in respect of that syndicate and year. This defence failed. The Master of the Rolls said this on construction:*

> *"Courts will never construe words in a vacuum. To a greater or lesser extent, depending on the subject matter, they will wish to be informed of what may variously be described as the context, the background, the factual matrix or the mischief. To seek to construe any instrument in ignorance or disregard of the circumstances which gave rise to it or the situation in which it is expected to take effect is in my view pedantic, sterile and productive of error. But that is not to say that an initial judgment of what an instrument was or should reasonably have been intended to achieve should be permitted to override the clear language of the instrument, since what an author says is usually the surest guide to what he means. To my mind construction is a composite exercise, neither uncompromisingly literal nor unswervingly purposive: the instrument must speak for itself, but it must do so in situ and not be transported to the laboratory for microscopic analysis."*
>
> *"I readily accept Mr Eder's submission that the starting point of the process of interpretation must be the language of the contract. But Mr Eder went further and said that, if the meaning of the words is clear, as he submitted it is, the purpose of the contractual provisions cannot be allowed to influence the court's interpretation. That involves approaching the process of interpretation in the fashion of a black-letter man. The argument assumes that interpretation is a purely linguistic or semantic process until an ambiguity is revealed. That is wrong. Dictionaries never solve concrete problems of construction. The meaning of words cannot be ascertained divorced from their context. And part of the contextual scene is the purpose of the provision. In the field of statutory interpretation the speeches of the House of Lords in* ***A.G. v Prince Ernest Augustus of Hanover*** *[1957] A.C. 436 showed that the purpose of a statute, or part of a statute, is something to be taken into account in ascertaining the ordinary meaning of words in the statute: see Viscount Simonds' speech, at 461, and Lord Somerville of Harrow's speech, at 473. It is true that such a purpose may also be called in aid at a later stage in the process of interpretation if the language of the statute is ambiguous but it is important to bear in mind that the purpose of the statute is a permissible aid at all stages in the process of interpretation. In this respect a similar approach is applicable to the interpretation of a contractual text. That is why in* ***Reardon Smith Line Limited v Yngvar Hansen Tangen*** *[1976] 1 W.L.R. 989 Lord Wilberforce, speaking for the majority of their Lordships, made plain that in construing a commercial contract it is always right that the court should take into account the purpose of a contract and that presupposes an appreciation of the contextual scene of the contract.*

Corbin on Contracts, 1960, Volume 3, s 545, explains the role that the ascertainment of the purpose of a contract should play in the process of interpretation:

> *"In order to determine purposes we are obliged to interpret their words in the document of agreement and their relevant words and acts extrinsic to that document. It may seem foolish, therefore, to say that the words of a contract should be interpreted in the light of the purposes that the parties meant to achieve, when we can turn on that light only by process of interpretation. Nevertheless, it is believed that such an admonition serves a useful purpose. As the evidence comes in and as interpretation is in process, the court may soon form a tentative conviction as to the principal purpose or purposes of the parties. As long as that conviction holds (and the court must be ready at all times to be moved by new evidence), further interpretation of the words of contract should be such as to attain that purpose, if reasonably possible."*

In the same section of this seminal work the author added that if the court is convinced that it knows the purpose of the contract, however vaguely expressed and poorly analyzed, it should be loath to adopt any interpretation of the language that would produce a different result. In my judgment these observations accurately state the approach to be adopted. And in the present case the purpose of clause 9 (c) is not in doubt."

Steyn L.J's application of this approach is of note: *"The implications of the agents' argument that clause 9 (c) precludes the Names from suing the agents for negligence so long as a cash call in respect of syndicate and year account remains outstanding generates immediate scepticism. This is an invitation to adopt an interpretation which is at variance with the purpose of clause 9 (c). This interpretation achieves something that is commercially unnecessary and different from the acknowledged purpose of clause 9 (c). It amounts to saying that clause 9 (c) has the coincidental or collateral effect that the agent is protected against actions in negligence while a cash call remains unpaid. Furthermore, as Mr Boswood Q.C. said, the agents' interpretation leads to the extraordinary result that if the agent ruins a Name by negligent underwriting, so that the Name cannot pay the cash call, the contract breaker or tortfeasor goes scot-free. And that result is inimical to the interests of policyholders and the Lloyd's market since the claim*

against the agent may be an asset available to meet the policyholders' claims. That is so uncommercial and unreasonable a result that words of the greatest precision would be required to achieve it. Clause 9(c) plainly comes nowhere near this."

Finally, Hoffman L.J. said this: "It seems to me legitimate to test the plausibility of a given construction by examining what the consequences would be. The construction for which the Agents contend means that if they are going to be negligent, they should rather ruin their Names entirely than leave them with enough resources to pay their calls. In the latter case they will be exposed to an action for negligence whereas in the former case they will be immune. Mr Eder said that his startling consequence had to be accepted in the interests of maintaining discipline at Lloyd's and inducing the Names to pay their calls. But his argument cannot apply to those who have no money. And in cases of contumacious refusal to pay, it is hard to see why denial of the right to sue for negligence will be more effective than the undisputed right of Lloyd's to obtain judgment for the unpaid calls.""

12. Although each of the extracts in the judgment in the Court of Appeal is very helpful and is directly relevant to the interpretation of a contract of this kind, nevertheless it did not seem to me that any of them set out any new principle or proposition. Mr Reese QC accepted that this was so but, of course, their value is not diminished. It may however explain why the decision had not been reported.

13. The parties agreed that the issues should be approached in reverse order and accordingly I begin with Issue 3.

Issue 3. Whether the plaintiffs liability for defects in design was limited in the manner alleged by the plaintiff in paragraph 50A of the .Amended Reply and Defence to Counterclaim.

This issue clearly required a consideration of the whole of the contract, but argument focused particularly on the following clauses. (I have emphasised in italics the key provisions relevant to Issue 3. Provisions relevant only to other issues are set out later.)

"SECTION 1 - DEFINITIONS AND STANDARD TERMS

1.1 DEFINITIONS

Words and phrases used throughout this Agreement shall have the following meanings:

(a) "Acceptance" means the date on which the COMPANY gives written notice to CONTRACTOR that it is satisfied that CONTRACTOR has performed the Work in accordance with all requirements contained in this Agreement as far as can be determined by COMPANY. Acceptance or payment by COMPANY hereunder shall in no way relieve CONTRACTOR of any obligation or liability under this Agreement. .....

(k) "Design" shall mean any design engineering, draughting and detailing by CONTRACTOR required to complete the Work in accordance with this Agreement.

(n) "Facility" means that property of the Group (including all materials), the object or result of any part of the Work, which is intended to be a part of the Group's oil production platforms located in Blocks 3/3 and 3/8a of the UK Sector of the North Sea. The complete facility is referred to generally in the specification as existing equipment to be modified, new equipment to be installed and all associated pipework, fittings, fixtures, components and equipment associated with the accommodation of third party entrant subsea completions and produced hydrocarbons or gas on the existing Ninian Field platforms. .....

(p) Throughout this Agreement, "Group" means such companies in addition to COMPANY as may from time to time hold any interest in United Kingdom Production Licence(s), petroleum field(s) or prospect(s) with which work is associated or in the petroleum produced or to be produced therefrom. On request but without prejudice to the foregoing, CONTRACTOR may obtain current details of the Group applicable to any Work.

(s) "material" and "materials" mean all materials, supplies and equipment to be incorporated into the Facility, unless the context requires otherwise. .....

(y) "Segment" means a portion of the Work capable of being placed into service by itself, or with previously completed Segments. Each CTR workscope shall be considered as a "segment".

(ee) "Work" means any and all work to be performed by CONTRACTOR under this Agreement, unless the context requires otherwise."

SECTION 2 - GENERAL REQUIREMENTS

2.1 CONTRACTOR'S SCOPE OF WORK

Except as otherwise provided in Section 2.4 or 22 hereof, CONTRACTOR shall perform all designs, prepare all records, furnish all supplies and all items of a consumable nature that are required for design of the Facility in this Agreement and the documents listed immediately below which are an integral part of this Agreement and such additional explanations as COMPANY shall furnish to CONTRACTOR to detail the requirements of this Agreement.

Exhibit I Scope of Work
Exhibit II Basis of Compensation
Exhibit III Incentive Programme
Exhibit IV Project Organisation
Exhibit V Key Personnel

Exhibit VI Project Schedule
Exhibit VII Sub-Contractors
Exhibit VIII Performance Bond
Exhibit IX Personnel Section Criteria and Job Descriptions
Exhibit X Project Co-ordination Procedures

Volume II CONTRACTOR'S CTR Catalogue

Without prejudice to the generality of the foregoing, CONTRACTOR's scope of work shall include activities, as detailed in Exhibit I, all to be performed to the satisfaction of the COMPANY's Representative.

CONTRACTOR shall perform the Work with due diligence and in accordance with generally accepted, current good practice of the industry and trades involved, Furthermore;

(a) The Facility shall be of a design which will meet the requirements of this Agreement, provide high operating reliability, minimum downtime inoperable and achieve an economical balance of first cost versus operating and maintenance cost.

(c) COMPANY does not desire to place restrictions on CONTRACTOR's judgment as to design of the Facility. In the interpretation of the design requirements of this Agreement, it is not intended that there be imposed on CONTRACTOR any design condition which is inconsistent with sound economics or good design practice. If in CONTRACTOR's judgment such inconsistencies develop, CONTRACTOR shall immediately notify COMPANY and, if COMPANY concurs with CONTRACTOR's judgment, a jointly acceptable modification of this Agreement will be issued pursuant to Section 2.5 hereof.

(d) CONTRACTOR shall perform the Work with diligence and in accordance with generally accepted, current, good practice of the industry and trades involved. Furthermore, CONTRACTOR shall ensure that the Facility:
i) complies with the requirements of this Agreement;
ii) is complete in every respect in the manner indicated or manifestly implied in this Agreement;
iii) is able to operate satisfactorily in all conditions that may be encountered within the design parameters;
iv) is safe to operate and maintain; and
v) meets all requirements for the obtaining of a Certificate of Fitness.
vi) meets the approval of Lloyd's, and DoT or any other Statutory or Regulatory Authority.

CONTRACTOR's performance and the Facility shall comply with the provisions of this Section regardless of whether or not full details of such practice or completeness are contained in this Agreement and provided COMPANY and CONTRACTOR shall agree on any such requirements. .....

2.6 PRECEDENCE

In the event of a conflict between any of the following items, they shall take precedence in the order listed:
a) Sections 1 through 31 hereof.
b) Exhibits attached hereto.
c) Standard drawings in the Specification.
d) American Society of Testing Materials Specifications, British National Standards, the National Electrical Code or other similar publications referred to in the Agreement but not included in the Appendix of the Specification.
e) CONTRACTOR's design, drawings, data and/or specifications. .....

SECTION 3 - PERFORMANCE OF THE WORK

3.1 DRAWINGS - DESIGNS

3.1.1 Designs by Contractor

a) In the planning and execution of the Work hereunder CONTRACTOR shall perform all engineering activities required to establish the suitability of CONTRACTOR's methods and equipment and to clarify, detail or otherwise facilitate the Work, or field revisions thereto.

b) CONTRACTOR shall use those COMPANY standard drawings which are requirements of this Agreement. CONTRACTOR may substitute its own standard drawing for a given COMPANY standard drawing only upon prior written approval of COMPANY. If such approval is given, CONTRACTOR's standard drawing shall be deemed a COMPANY standard drawing for the purpose of Section 2.6 hereof.

c) As soon as completed and checked by CONTRACTOR prints of CONTRACTOR's drawings, including subsequent revisions thereto and including CONTRACTOR's standard drawings shall be given to COMPANY for review and approval. At the start of work, COMPANY will advise CONTRACTOR which drawings, if any, do not require COMPANY approval. Within ten (10) working days of receipt of the prints, COMPANY will advise CONTRACTOR of comments it has, will request any additional date it may require or will approve the drawings. .....

g) As soon as CONTRACTOR's design and fabrication drawings have been approved for construction CONTRACTOR shall produce photographically reduced copies at A3 size of all significant drawings as agreed with COMPANY's Representative. Ring bound copies of the A3 prints shall be issued to COMPANY. Subsequent significant drawing revisions shall also be reduced to A3 size by CONTRACTOR.

3.1.2 Drawings and Designs provided by COMPANY

(c) CONTRACTOR shall be responsible for verifying all dimensions of and proper fitting up of tie-ins to existing facilities or facilities to be constructed by others as shown on the design drawings provided by COMPANY based on an offshore survey report. CONTRACTOR shall submit any proposed change or deviation from drawings to COMPANY for written approval before fabrication or installation.

3.1.3 As-Built Drawings

During construction CONTRACTOR shall keep on file in its project office current markups of all drawings to agree with the actual installation. CONTRACTOR shall revise the originals of all significant drawings (eg P & ID's plot plans, electrical single line diagrams, equipment data sheets, and vessel drawings) upon completion of each Segment and deliver these to COMPANY at the same time as delivering the Segment to agree with actual installation. Minor construction drawings, such as piping spools and structural details, need to be revised. Revisions to models, if any, are not required.

COMPANY will maintain a representative ("COMPANY's Representative") who will be the only COMPANY employee authorised to represent COMPANY with respect to this Agreement. His functions, which he may from time to time delegate in writing to others, shall include but not be limited to:

i) Establishing and maintaining liaison between CONTRACTOR's Representative and COMPANY.

ii) Reviewing CONTRACTOR's schedule and performance.

iii) Making such inspections as COMPANY may desire in order to check the progress and quality of the work.

iv) As a result of Variations pursuant to Section 2.5 hereof, negotiate and subject to COMPANY Management approval agreeing any consequent change in remuneration or Completion Date.

After the start of Work, COMPANY's Representative will assist CONTRACTOR in developing procedures for handling correspondence, approving purchases, approving CONTRACTOR's programmes, personnel requirements, etc., reviewing CONTRACTOR's plans for recruiting skilled personnel in critical disciplines, reviewing and approving CONTRACTOR's subcontracting plans, subcontractor's manpower requirements, and other administrative aspects of the Work. Such assistance shall in no way detract from CONTRACTOR's status hereunder as an independent CONTRACTOR.

CONTRACTOR shall provide office space, office furniture, local and long distance telephone, facsimile and telex service, and other such services for COMPANY's Representative and other COMPANY and third party personnel throughout the course of the Work.

c) <u>CONTRACTOR's Representative</u>

CONTRACTOR shall maintain a representative ("CONTRACTOR's Representative") at all times and at all locations when Work is in progress who shall act in full charge of CONTRACTOR's work and maintain liaison between CONTRACTOR and COMPANY's Representative. His functions, which he may from time to time delegate to others, shall include but not be limited to:

i) Establishing and maintaining liaison between COMPANY's Representative and CONTRACTOR.

ii) Representing CONTRACTOR in matters pertaining to performance and quality, scheduling and accounting practices.

iii) As a result of Variations pursuant to Section 2.5 hereof, negotiating and approving any consequent change in remuneration or Completion Date.

CONTRACTOR shall not change its Representative during the course of the Work unless COMPANY approves such change in writing.

a) COMPANY and others responsible to COMPANY shall have the right, but not the obligation, to inspect the Work or any part thereof, at all times, and CONTRACTOR shall provide proper facilities therefor. CONTRACTOR shall at all times during working hours keep a competent person in the immediate vicinity of each area in which any part of the Work is being performed to receive communications from COMPANY and to supervise that part of the Work.

b) CONTRACTOR shall be solely responsible for the quality of the Work. COMPANY will make such inspection as COMPANY may desire in order to check the progress and quality of the work, to see that CONTRACTOR's employees are properly qualified in their respective discipline, that workmanship is of an acceptable grade, and that all requirements of this Agreement are being met. Such inspection or any other inspection by COMPANY shall not relieve CONTRACTOR of full responsibility for the performance of its obligations under this Agreement.

CONTRACTOR shall fully co-operate with COMPANY and any other CONTRACTOR employed by COMPANY to ensure that all parts of the Work being carried out at the Site are correctly integrated (where necessary) with other services supplied by COMPANY or any other CONTRACTOR and that the overall programme (as indicated on or deduced from Exhibit VI - Project Schedule) is achieved. In the event that CONTRACTOR has any grievance about the lack of co-operation on the part of other CONTRACTORS (not being contractors for which it is responsible hereunder) CONTRACTOR shall immediately notify COMPANY's Representative thereof. Should CONTRACTOR be delayed in the performance of the Work by the lack of co-operation on the part of the other said CONTRACTORS then such delay shall be treated as if it were caused by CONTRACTOR unless COMPANY's Representative shall have been notified as aforesaid.

It is agreed that the performance of portions of the Work by Subcontractors and the performance of other work by other contractors may result in programming conflicts. If such conflicts arise they shall be resolved so as to result firstly in the maximum probability of the overall programming being achieved and secondly in the performance of the greatest amount of work during the conflict. It is further agreed that the consequences of such resolution of any such programming conflicts have been adequately allowed for in the overall programme, in Exhibit VI - Project Schedule and in all other ways.

a) The Work shall be considered complete only when CONTRACTOR has met all requirements of this Agreement to the satisfaction of COMPANY.

b) When CONTRACTOR considers that a Segment of Phase I, II or III described in EXHIBIT I - SCOPE OF WORK are completed in accordance with the requirements of this Agreement, CONTRACTOR shall so notify COMPANY in writing. After receipt of such notice, COMPANY shall have thirty (30) days to review and inspect the completed Work as to conformance to the requirements of this Agreement. At or prior to the end of such period, COMPANY's Representative will either advise CONTRACTOR in writing of any defects or deficiencies it has discovered in such Work. CONTRACTOR shall promptly correct such defects or deficiencies at no additional cost to COMPANY.

c) Upon completing all corrective Work, CONTRACTOR shall again so notify COMPANY in writing and COMPANY shall review and accept or reject such corrective Work as outlined in Subsection 3.4.1(b) above. CONTRACTOR shall not be entitled to any costs whatsoever incurred in the performance of corrective Work.

d) Acceptance by COMPANY or payment hereunder shall in no way relieve, reduce, modify or affect any obligation or warranty of CONTRACTOR whether under this Agreement and/or at law or otherwise.

a) COMPANY's notice of Acceptance of a Phase, issued pursuant to Subsection 3.4.1 shall establish the date of Acceptance of such Segment. The date of completion of a Phase may be varied pursuant to Section 8.

b) Until COMPANY has issued a written notice of Acceptance the Work shall not be considered accepted either in whole or in part. Neither payments made during the performance of the Work, nor the presence of COMPANY's Representative during the course of the Work, shall constitute Acceptance of the Work or of any part of the Work.

c) Acceptance of all or any Segment or Segments by COMPANY notice shall not release CONTRACTOR from any liability or obligation which has been incurred by CONTRACTOR under this Agreement prior to the issue of such notice of Acceptance, including but not limited to the requirements of Subsection 3.4 herein.

3.4.3 Guarantees

With respect to any Designs, data or information which have been provided, reviewed or approved by COMPANY, CONTRACTOR guarantees each Segment to be free of defects in CONTRACTOR furnished Design, and CONTRACTOR guarantees corrective Work, if any, performed by CONTRACTOR hereunder to be free of defects in design.

This guarantee does not apply to defects caused by the Facility being subjected to conditions substantially more severe than described in this Agreement.

COMPANY shall notify CONTRACTOR in writing or by telephone or telex confirmed in writing whenever a breach of this guarantee exists, and CONTRACTOR shall be given reasonable opportunity if in the opinion of the COMPANY the nature of the defect and COMPANY's operating schedule permit, to inspect and correct such defective Design, and any portion of the Facility damaged by the defect or by repair of it. Prior to start of any work pursuant to this guarantee, CONTRACTOR shall inform COMPANY of the nature of corrective work which CONTRACTOR proposes to perform and shall obtain COMPANY's approval thereof.

When required by COMPANY, corrective work required to satisfy this guarantee shall be performed on an overtime and/or shift basis and using the fastest means available in order to minimise COMPANY's loss of operating time. In any event any corrective work performed under this Guarantee shall be entirely at CONTRACTOR's expense as regards the supply of materials and labour.

COMPANY shall have the right to have corrective work performed by others, but should COMPANY exercise such right CONTRACTOR's obligations under this guarantee shall be limited to payment of the actual direct cost of such corrective work. .....

SECTION 9 – LIABILITY .....

9.4 CONTRACTOR shall exercise due care and diligence in the performance of this Agreement and in the design of the Facility and CONTRACTOR shall be liable for and shall indemnify the Group against losses, damages, compensation, claims, demands, proceedings, costs, charges and expenses in respect of each event of loss, damage or destruction of any property of the Group (including the Facility), caused by or arising out of the act, neglect, default or omission of CONTRACTOR regardless of negligence and any other liability of COMPANY or the Group in tort contract, under statute or otherwise, provided always, CONTRACTOR's liability to COMPANY and the Group hereunder shall be limited to One Million Pounds Sterling (£1,000,000) in respect of any one event and unlimited in all. CONTRACTOR shall have no such liability unless COMPANY shall have given to

CONTRACTOR written notice of the liability within two (2) years from the date of commissioning of any objects on the Facility produced from CONTRACTOR's design or three (3) years from mechanical completion and commissioning thereof whichever is the earlier.

14. I here interpose to record that by Variation Order 14 Foster Wheeler and Chevron agreed that the scope of the works would be changed and the terms of clause 9.4 would be modified as follows:-

"From February 13 1993, all CONTRACTOR's reimbursable personnel will form an integrated team with COMPANY's personnel to carry out the follow-on engineering scope of work. This team shall take instructions from and report directly to COMPANY's personnel under direction of COMPANY's Representative. .....

COMPANY AND CONTRACTOR AGREE THAT THE TERMS AND CONDITIONS OF CONTRACT ARE CHANGED AS FOLLOWS:

With respect only to work done by the Integrated Project Team the following aspects are removed from the CONTRACTOR's responsibilities:
(a) Section 3.1 Drawings-Designs
(b) Section 3.3.2 Inspection
(c) Section 3.4 Completion, Acceptance and Guarantees

Section 9.4 is renumbered 9.4(a).

New Section 9.4(b) is added as follows:

9.4(b) Notwithstanding the provisions of Section 9.4(a)

15. *I now revert to the extracts from the contract.*

"9.7 Notwithstanding anything to the contrary contained herein, as between COMPANY and CONTRACTOR, it is agreed that the responsibility for pollution or contamination shall be as follows:
a. CONTRACTOR shall assume responsibility and liability for pollution or contamination caused by or arising out of the act, neglect, default or omission of CONTRACTOR or its Subcontractors including control and removal of the same for an amount up to Five Hundred Thousand Pounds Sterling (£500,000) in respect of any one event. COMPANY shall indemnify CONTRACTOR for any liability in excess of said amount.

9.8 Neither Party or its Subcontractors or the Group shall be liable for any loss of contract, product, production or profit, business interruption and similar form of consequential damage suffered by either party or its Subcontractors or the Group. .....

SECTION 12 - ACCEPTANCE/REJECTION

12.1 At any time prior to Date of Acceptance of the Facility or of a Segment of Work, COMPANY may reject work provided by CONTRACTOR and parts of the Work or such Segment which are defective or fail in any way to conform with the requirements of this Agreement. As soon as practicable after receiving notice thereof from COMPANY, CONTRACTOR shall at CONTRACTOR's expense remove and replace such Work and reperform the Work necessarily affected by such removal and replacement. After Acceptance of the Work or of any Segment, and portions of the Work which fail to meet the guarantees stated in Section 3.3.2 hereof shall be replaced or reperformed in accordance with the provisions of said guarantees.

12.2 When CONTRACTOR considers that it has fully performed a Segment of the Work it shall issue notice to COMPANY of completion with respect to that Segment. Such notice shall be supported by relevant documentary evidence. Within thirty (30) days of receipt of CONTRACTOR's completion notice COMPANY shall notify CONTRACTOR of deficiencies that COMPANY require to be remedied or COMPANY shall issue Acceptance.

SECTION 28 - PARTICIPANTS CLAUSE

28.1 For the purposes of sub-sections 28.2 and 28.4 hereunder of this section it is agreed that:-
(a) this Agreement has been made by COMPANY not only on it own behalf but also as agent and trustee for the Members from time to time of the Ninian Group and each of them;
(b) such Members are, or, if not presently Members, shall on ratification or adoption become, parties to this Agreement;
(c) such members shall be bound by and entitled to the benefit of the provisions of sub-section 28.2 through 28.4 hereunder but shall not otherwise be under any obligation of liability whatsoever to the CONTRACTOR however arising.

28.2 In consideration of the provisions of this Section the Members of the Ninian Group sanction the making of this Agreement by COMPANY.

28.3 If any loss, damage, injury or expense should be caused to the said Members or any of them by any breach of this Agreement by the CONTRACTOR or any tort of the CONTRACTOR or those for whom he is responsible or if any situation should arise or event occur which directly or indirectly gives rise to an obligation on the part of the CONTRACTOR under this Agreement to indemnify the COMPANY or the said members or any of them:-

(a) Subject to (b), (c) and (d) hereof, the CONTRACTOR shall be liable in damages to or, as the case may be, liable to indemnify the members and each of them;

(b) the CONTRACTOR shall be entitled as against the members to rely upon any defences or limitations or exclusions of liability which he is given by this Agreement;

(c) provided that the procedure of the relevant court so permits, the member shall not seek to enforce such liability or commence proceedings in their own names and any claims shall be made and proceedings brought by and the name of COMPANY alone claiming and/or suing as agent and/or trustee for the members and COMPANY shall be entitled to, and shall, on their behalf recover from the CONTRACTOR the full amount of their loss, damage, injury or expense and of their rights of indemnity.

(d) the provisions of this Agreement with regard to governing law and/or jurisdiction and/or arbitration shall apply to any such claims or proceedings in the same way as they apply where COMPANY is concerned solely on his own behalf."

16. As I have already indicated, Exhibit I set out the Scope of the Work, and outlined the contents of each of the three Phases. The text relating to Phase II - Detailed Engineering Work - reads as follows:-

"Subject to satisfactory performance and agreements of CTRs CONTRACTOR will be instructed to proceed with the Phase II work which will include the following:
(a) Final design engineering:- final plot plans, general arrangements, schematics, loop diagrams, isometrics, fabrication drawings, etc
(b) Final critical path network.
(c) Project planning bar charts.
(d) Project costing and Budgetary control.
(e) Vendor and Fabricator technical appraisal of tenders.
(f) Preparation of various material requisitions.
(g) Preparing tender package for fabrication, services, etc.
(h) Preparing tender packages for installation.
(i) Hazop study and formal safety assessments.
(j) Operation manuals and commissioning manuals."

The content of Phase III - Follow on Support Services - was described as follows:

"Subject to satisfactory performance and agreement of CTRs, CONTRACTOR will be instructed to provide Follow on Support Services CONTRACTOR's responsibilities may include the following with respect to the Project:
(a) Supplying site query support;
(b) Supplying engineering support at fabrication sites;
(c) Providing office support for field material requisitioning;
(d) If requested providing testing and inspection of assistance at manufacturers' works, at fabrication sites and off shore; and
(e) Correcting and updating all drawings approved for construction to "as built" condition.
(f) Correcting and updating all construction drawings to "as built" condition.
(g) Preparing response and supporting documentation for site queries.
(h) Providing engineering assistance with inspection and testing equipment of manufacturers' works.
(i) Providing on-site engineering assistance for fabrication direction and load out.
(j) Providing assistance to construction for field material requisitions resulting from site queries.
(k) Co-ordinating design site queries with other COMPANY Contractors, including:
- fabrication contractor;
- installation and hook-up and commissioning contractors; and
- subsea installation contractor.

All such Follow on support services shall be in accordance with CTRs to be agreed between COMPANY and CONTRACTOR prior to commencement of Follow-on Support Services."

17. Exhibit III to the contract was headed "Incentive Programme" and formed part of Exhibit II. It is not necessary at this stage to set out its text in full. It contained provisions for rewarding Foster Wheeler for consistently good progress and performance and for the formation of an Evaluation Team which would meet monthly to review progress and, amongst other things, to "agree man-hours for subsequent CTR workscopes". In paragraph 3 provision was made for a Progress Incentive whereby if the Programme Evaluation Team thought that Foster Wheeler had performed satisfactorily, then Foster Wheeler would be paid the management fee rate per hour for each direct man-hour saved in the achievement of any CTR workscope. However if a CTR workscope were not completed within the times agreed and set out in the Project Programme such a payment would not be made. Furthermore "in the event that on any CTR workscope, the CONTRACTOR expends manhours in excess of those agreed by the programme evaluation team then the management fee relating to such additional manhours will not be payable to CONTRACTOR".

18. Exhibit IV dealt with the Project Organisation. It required Foster Wheeler to perform the engineering/design for Phases I, II and III with *"an integrated Task Force Team of experienced and qualified engineers drawn from its own resources"*. It continued:- *"A multi-discipline Team of Engineers and Designers will be mobilised for both Topsides and Sub-sea activities located in a dedicated Project Office in CONTRACTOR's offices at East Tullos. A dedicated area in this office will accommodate COMPANY personnel. The Task Force environment will provide a close working relationship with COMPANY."*

Provision was later made for organisation charts which had been structured with the following objectives, amongst others, in mind:- *"A close working relationship between the CONTRACTOR's Task Force and the COMPANY Project Team" and "a single commercial and contractual interface, ...allowing a complete freedom for direct technical interface between COMPANY and the CONTRACTOR's Project Team Members".*

19. The scope of the contract and its structure and terms may therefore be seen to be typical of oil industry construction contracts.

20. In order to understand the ambit of Issue 3 Foster Wheeler's counsel annexed to their skeleton arguments summaries of three of the instances relied upon by Chevron in support of its claim that there have been design errors. The summaries prepared by Mr Reese and Mr Lofthouse are helpful, but in referring to them I shall leave out Foster Wheeler's answer since it is Chevron's claim which has alone to examined against Foster Wheeler's defence that it is not liable for it under the terms of the contract. However both Mr Reese and Mr White were at pains to emphasise that no decision was required or to be given on any of the questions of fact. Nothing in this judgment is therefore to be read as such a finding, eg as to whether Chevron decided to operate a contractual provision.

21. Re-work Claim 004 is based upon the discovery by Chevron during pre-commissioning of the gas compressors in module 38 that manual reset solenoids as specified by Foster Wheeler had been installed for PLC control start-up sequence valves instead of auto reset solenoids. Foster Wheeler proposed a solution which was to buy and install conversion kits to allow the change from manual to auto reset. The claim therefore comprised engineering costs incurred both by Foster Wheeler and Chevron and construction costs i.e. the cost of Chevron's installation contractor in carrying out the conversion work and using additional materials together with material costs.

22. Re-work Claim 007 arose out of what is alleged to be a unilateral change by Foster Wheeler which modified the scope of work required in the manufacture of liquified petroleum gas export pumps. It seems that, as a result, according to Chevron, the pumps were supplied without casing drain connections. These drain connections were therefore provided at additional cost so that Chevron's claim includes that cost and in addition engineering costs incurred by Foster Wheeler and Chevron in considering the question and resolving it with the manufacturer, Sulzer (UK) Pumps Ltd.

23. Re-work Claim 025 concerns an alleged error which led to the rooting of a 20 inch pipeline in the flare pipe work on module 06 clashing with the existing main tubular steel work. Chevron maintained that Foster Wheeler failed to provide a properly co-ordinated design. The result, according to Chevron, was that the pipe spools had to be modified. This required the spools that had been installed to be removed and reconstructed using additional materials. Additional hydro-testing had also to be carried out. Chevron therefore maintained that they incurred some engineering time (very small), some substantial construction costs and some (minimal) material costs.

24. Reference was also made to a similar re-work claim 002.

Essentially the types or heads of cost or expense said to have been incurred by Chevron include:

1. considering a problem and deciding whether it was a design error and if so what ought to be done about it (the cost here may have been incurred both by Foster Wheeler and by Chevron);

2. re-designing the relevant part of the work (again this may have been carried out by Foster Wheeler rather than Chevron), together with, if necessary, and where appropriate, the cost of the time spent by Chevron on supervising and approving the new proposals;

3. putting right the error by way of additional fabrication or installation costs, including the cost of additional or replacement materials; this would affect
   (a) the work as originally designed;
   (b) work affected by the error e.g. testing or having to re-test work which was of itself unaltered;

4. revising the drawings so that they reflected the "as built" condition.

In addition I shall assume that Chevron may have incurred other costs and losses although they do not appear clearly from any of the examples relied on by Foster Wheeler.

25. Foster Wheeler's arguments, in summary, were that the contract had been carefully drawn up and that it was clear from reading its provisions as a whole that the parties had set out a comprehensive code for what was to happen should a flaw be discovered in Foster Wheeler's work both on the basis that it would not give rise to a breach of the agreement, and more particularly, on the basis that it would constitute a breach of the agreement and therefore of Foster Wheeler's primary obligations. Thus, it was argued, the code also dealt with the secondary obligation to compensate Chevron for any loss or damage that it might suffer from breach of Foster Wheeler's primary obligation. For convenience I shall refer to these flaws as defects by which I mean that some aspect of the product of Foster Wheeler's engineering and other obligations was not in accordance with the contract. Part of Foster Wheeler's obligations included presenting Chevron with its proposals for approval. The term "defect" therefore covers any flaw or error then discovered which had to be put right before Chevron could approve the drawing etc. Use of this working definition could imply that Foster Wheeler were then in breach of contract. In ***P and M Kaye Ltd v Hosier & Dickinson Ltd*** [1971] 1 WLR 146 Lord Diplock said at page 165 that work done during the course of a building contract which did not comply with its terms but which was remedied by the contractor in a timely manner before completion without loss to the employer beyond perhaps delay in

completion should be regarded as a "temporary disconformity". Mr Reese QC submitted that ***Lintest Builders Ltd v Roberts*** (1980) 13 BLR 38 (CA) and ***Surrey Heath BC v Lovell Construction Ltd*** (1988) 42 BLR 25 and (1990) 48 BLR 108 (CA) had not decided that Lord Diplock's approach was wrong, and that slips on the part of Foster Wheeler which were or were capable of being picked up by Chevron during the course of the close working relationship contemplated by the contract could not be characterised as breaches of contract. For the purposes of Issue 3 I do not need to resolve his vexed point as I shall follow the views expressed in Hudson on Building Contracts, 11th ed at paragraphs 5-020 and 5-027-28 and in Keating on Building Contracts, 6th ed, at page 56 and proceed on the hypothesis that Foster Wheeler may be under a continuing duty to carry out work and to perform services so that, when done, and not merely on completion, the terms of the contract are met. Whether that duty exists, and the circumstances in which failure to observe it may constitute a breach of contract, will depend on further examination of the terms of the contract which may for example show that Chevron might suffer more than nominal loss and damage other than that arising from late completion (for example from the pleaded breaches of clause 3.1.2(c)). Even so, such a breach may still be a question of fact and degree. My working definition nevertheless necessarily assumes that Foster Wheeler might be in breach of contract despite the close contact that, according to the contract, ought to have taken place between Foster Wheeler and Chevron which was, as Foster Wheeler submitted - and I accept - intended to ensure that Foster Wheeler's work was, so far as practicable, defect-free. The methods of working described in the contract and in particular in Exhibit IV are of course commonplace in this sector of the oil industry.

26. Foster Wheeler's case was therefore that, accepting that clear words were required to limit liability, nevertheless the contract was sufficiently clear so as to limit Chevron's claims, essentially, to the ceiling on liability contemplated by clauses 3.4.3 and 9.4. Mr Reese relied inter alia on ***National Coal Board v William Neill*** [1985] QB 300 in support of the argument that a clear intention may be expressed without additional exclusionary words (see page 109F). Chevron's argument started from the opposite position, as it were. It maintained that a party such as Chevron was entitled to recover damages for breach of contract *unless* Foster Wheeler could show that the requisite clarity of language had been used whereby Chevron's rights to full damages were limited.

27. The contract and clauses in question do not, for present purposes, purport to exclude liability but rather only to limit Chevron's rights to recover all that they might otherwise be entitled to as damages for breach of contract. There was essentially common ground between the parties as to the principles of law applicable: the issue turned upon whether there was sufficient clarity of language. There was no dispute that the observations of Lord Diplock in ***Modern Engineering (Bristol) Ltd v Gilbert-Ash (Northern) Ltd*** at pages 717H and 718D applied:-

"It is, of course, open to parties to a contract for sale of goods or for work and labour or for both to exclude by express agreement a remedy for its breach which would otherwise arise by operation of law or such remedy maybe excluded by usage binding upon the parties (cf. Sale of Goods Act 1893, section 55). But in construing such a contract one starts with the presumption that neither party intends to abandon any remedies for its breach arising by operation of law, and clear express words must be used in order to rebut this presumption. In the case of building contracts no question of usage arises to rebut the presumption. ..."

"So when one is concerned with a building contract one starts with the proposition that each party is to be entitled to all those remedies for its breach as would arise by operation of law, including the remedy of setting-up a breach of warranty in diminution or extinction of the price of materials supplied or work executed under the contract. To rebut that presumption one must be able to find in the contract clear unequivocal words in which the parties have expressed their agreement that this remedy shall not be available in respect of breaches of that particular contract."

Mr White relied upon those passages and upon ***Ailsa Craig Fishing Co. Ltd v Malvern Fishing Co. Ltd*** [1983] 1 WLR 964. The speeches of Lord Wilberforce and of Lord Fraser of Tulleybelton are pertinent to the questions before me. Lord Wilberforce at page 966G said:-

"Whether a clause limiting liability is effective or not is a question of construction of that clause in the context of the contract as a whole. If it is to exclude liability for negligence, it must be most clearly and unambiguously expressed, and in such a contract as this must be construed contra proferentem. I do not think that there is any doubt so far. But I venture to add one further qualification, or at least clarification: one must not strive to create ambiguities by strained construction, as I think that the appellants have striven to do. The relevant words must be given, if possible, their natural, plain meaning. Clauses of limitation are not regarded by the courts with the same hostility as clauses of exclusion: this is because they must be related to other contractual terms, in particular to the risks to which the defending party may be exposed, the remuneration which he receives, and possibly also the opportunity of the other party to insure."

28. Lord Fraser of Tullybelton said at page 969H-970F:-

"The question whether Securicor's liability has been limited falls to be answered by construing the terms of the contract in accordance with the ordinary principles applicable to contracts of this kind. The argument for limitation depends upon certain special conditions attached to the contract prepared on behalf of Securicor and put forward in their interest. There is no doubt that such conditions must be construed strictly against the proferens, in this case Securicor, and that in order to be effective they must be "most clearly and unambiguously expressed": see ***W.& S. Pollock & Co. v Macrae,*** *1922 SC (HL) 192 at page 199 per Lord Dunedin.* ***Pollock*** *was a decision on an exclusion clause but in so far as it emphasised the need for clarity in clauses to be construed contra proferentem it is in my opinion relevant to the present case also. It has sometimes apparently been regarded as laying down, as a proposition of law, that a*

clause excluding liability can never have any application where there has been a total breach of contract, but I respectfully agree with the Lord President who said in his opinion in the present case that that was a misunderstanding of Pollock. Pollock was followed by the Second Division in ***Mechans Ltd v Highland Marine Charters Ltd.,*** *1964 SC 48 and there are passages in the judgments in that case which might seem to treat* ***Pollock*** *as having laid down some such general proposition of law, although it is not clear that they were so intended. If they were I would regard them as being erroneous.* ***Mechans*** *appears to have been relied upon by counsel for the appellants before the Second Division, but was not relied on in this House.*

There are later authorities which lay down very strict principles to be applied when considering the effect of clauses of exclusion or of indemnity: see particularly the Privy Council case of ***Canada Steamship Lines Ltd v The King*** *[1952] A.C.192, 208, where Lord Morton of Henryton, delivering the advice of the Board, summarised the principles in terms which have recently been applied by this House in* ***Smith v U.M.B. Chrysler (Scotland) Ltd.,*** *1978 SC (HL) 1. In my opinion these principles are not applicable in their full rigour when considering the effect of clauses merely limiting liability. Such clauses will of course be read contra proferentem and must be clearly expressed, but there is no reason why they should be judged by the specially exacting standards which are applied to exclusion and indemnity clauses. The reason for imposing such standards on these clauses is the inherent improbability that the other party to a contract including such a clause intended to release the proferens from a liability that would otherwise fall upon him. But there is no such high degree of improbability that he would agree to a limitation of the liability of the proferens, especially when, as explained in condition 4(i) of the present contract, the potential losses that might be caused by the negligence of the proferens or its servants are so great in proportion to the sums that can reasonably be charged for the services contracted for. It is enough in the present case that the clause must be clear and unambiguous."*

29. I was also referred to ***Billyack v Leyland Construction*** [1968] 1 WLR 471, and ***AMF International Ltd v Magnet Bowling Ltd*** [1968] 1 WLR 1028 at 1060D-G.

30. Although to answer Issue 3 (and the other issues) the contract has to be read as a whole it is convenient to examine the clauses principally relied on by Foster Wheeler to see what they cover and so to place them within the structure of the whole contract.

Clause 3.4.3

31. I start first with clause 3.4.3 not only because it was Foster Wheeler's case that clause 3.4.3 was the bench mark of their liabilities but also because it deals with the position post Acceptance and therefore with the time when typically defects which have not previously been picked up may be found and dealt with. In addition clause 3.4.3 has to be contrasted with clauses 9 and 12. (I approach clause 3.4.3 on the basis that notwithstanding Variation 14 it remained part of the contract.) The first paragraph of clause 3.4.3 is coextensive with and restates the effect of the primary obligations of Foster Wheeler which are to be found in for example, clause 2.2. It does not add anything to the obligation of Foster Wheeler to produce work and perform services which comply with the contract. It is a natural conclusion to clauses 3.4.1 and 3.4.2 (although Mr Reese QC accepted that there appears to be no practical distinction between Completion and Acceptance under the contract). In my judgment the remainder of clause 3.4.3 is equally clear as to what is to happen if a breach of the guarantee were to be found. Chevron has first to notify the Contractor of that breach. Thereafter Chevron has options.

32. First, if Chevron considers that the nature of the defect and its own operating schedule permit, then it is evidently obliged to give Foster Wheeler a reasonable opportunity to put right the defect. Foster Wheeler will then be under an obligation not merely to put right the defect but also to correct "*any portion of the Facility damaged by the defect or by repair of it.*" This appears to go further than perfecting Foster Wheeler's obligation to provide engineering services (by way of design of the modifications etc.). Mr White rightly submitted that Foster Wheeler's obligations were wider. It had to ensure that so far as its work was involved the Facility as a whole had been designed properly. Clause 2 requires Foster Wheeler to direct its work towards the design of the Facility (as defined in clause 1.1) to meet the requirements set out in, for example, clauses 2.1, 2.2 (a) and, in particular (d) (i) - (vi). It is therefore sensible to provide that if there has been a breach of the guarantee which manifests itself in some actual or prospective mal-operation of the Facility it is then incumbent on Foster Wheeler to put right not merely any design error but also its physical consequences. The fact that Foster Wheeler will not have originally undertaken fabrication or installation of work does not detract from the efficacy of this requirement as a company in the position of Foster Wheeler will engage the fabrication or installation contractor whose work is immediately affected to carry out the necessary modifications (just as Chevron would). Furthermore the fourth paragraph of clause 3.4.3 concludes by stating: *"in any event any corrective work performed under this guarantee shall be entirely at CONTRACTOR's expense as regards the supply of materials and labour"*. If Foster Wheeler could not engage contractors to carry out the necessary work and had to leave it to be arranged by Chevron, then the words which I have quoted would entitle Chevron to recover its costs, if not paid by Foster Wheeler, from Foster Wheeler.

33. Secondly, if it is not possible for Chevron to give Foster Wheeler the opportunity to put right the defect in the manner contemplated by the third paragraph of clause 3.4.3 then the fifth paragraph provides, in my judgment, for Chevron to have the necessary work carried out by others. The fifth paragraph states "COMPANY shall have the right to have corrective work performed by others, but should COMPANY exercise such right CONTRACTOR's obligations under this guarantee shall be limited to payment of the actual direct costs of such corrective work". It gives Chevron an unqualified right as there are no words of limitation which would indicate that the right can only be exercised if no reasonable opportunity could be given to Foster Wheeler to put right the defect. Chevron may

therefore "have corrective work performed by others" even if the nature of the defect and Chevron's operating schedule might well have permitted Foster Wheeler to have been given the opportunity to put right the defect.

34. However if Chevron were in effect not to follow up the notice given to Foster Wheeler of the defect by requiring it to put it right then the amount recoverable from Foster Wheeler is "limited to payment of the actual direct costs of such corrective work". Its purpose is to ensure that Foster Wheeler is not thereby worse off if Chevron do not give it the opportunity to do the work in that it will not have to pay for heads of costs which it would not have incurred had it been given the opportunity to carry out the work and had it done so. Chevron's actual direct cost is thus to be equated to the "expense" referred to in the preceding paragraph of clause 3.4.3 for if Foster Wheeler had carried out the corrective work it would have been liable for the types or heads of costs which I described under 1, 2, 3 and 4 above.

35. Chevron may of course be required to justify its actions if Foster Wheeler took the view that it was unreasonable for Chevron to act under the fifth paragraph and to require payment of "actual direct costs" which might be higher than the expense which Foster Wheeler would have borne had Chevron gone down the route of requiring Foster Wheeler to put right the defect.

36. In my judgment therefore clause 3.4.3 does not serve to limit Foster Wheeler's liability for a defect insofar as it extends to the types of cost described under 1, 2, 3, and 4 above in so far as they are likely to be incurred by either party.

37. Chevron may however have incurred costs or expense which were attributable to breach of the guarantee but which did not form part of the "expense" or "the actual direct costs", or if it is wrong completely to equate these concepts. Mr White drew attention to ***Millars Machinery Co. Ltd. v. David Way and Son*** (1934) 40 Com. Cas. 204, ***Saint Line Ltd. v. Richardsons Westgarth & Co. Ltd.*** [1940] 2 KB 99, and ***Croudace Construction Ltd. v. Cawoods Concrete Products*** (1978) 8 BLR 20 and submitted that the words "actual direct costs" would include all heads of cost which did not fall within the second limb of ***Hadley v Baxendale***. Mr White's submission has considerable force but the precise ambit of the words "actual direct costs" should not be decided hypothetically and I do not intend to do so. It is sufficient to note that Chevron might incur expense or suffer loss which under these words would not be recoverable from Foster Wheeler.

38. I reject the submission that if Foster Wheeler were to be required to carry out the corrective work then clause 3.4.3 would exclude the recovery of those heads of cost (assuming them otherwise to be recoverable and not barred by the contract or by operation of law). At first sight the last paragraph would appear to limit Chevron's rights but in my judgment it would be wrong so to confine that paragraph since the limitation applies only to "CONTRACTOR's obligations under this guarantee". Those obligations are to put right the defect when called upon so to do at the contractor's expense "as regards the supply of materials and labour". These are words of definition and not limitation and do not exclude Chevron's right to recover damages for what must be a breach of contract and which led it to exercise the first option. That right is, as Mr White correctly submitted, additional in the sense that without it Chevron would not be able to require Foster Wheeler to return after Acceptance, although the contract plainly envisages that the first option is the normal and preferred route as might be expected of a "Guarantee" (see clause 12.1). In addition Acceptance as such does not alter Chevron's rights in law. Clause 3.4.1(d) states: *"Acceptance by Company or payment hereunder shall in no way relieve, reduce or modify or affect any obligation or warranty of Contractor whether under this agreement and/or at law or otherwise."* (Mr White's emphasis added.)

39. Clause 3.4.2(c) provides: *"Acceptance of all or any Segment or Segments by Company notice shall not release Contractor from any liability or obligation which has been incurred by Contractor under this Agreement prior to the issue of such Notice of Acceptance, including but not limited to the requirements of Section 3.4 herein."* (Mr White's emphasis added.)

40. Mr White submitted that these provisions applied as much to Foster Wheeler's secondary obligation to pay damages as its primary obligations. In my judgment that is correct. These clauses preserve Chevron's right to sue Foster Wheeler for damages for breach of any primary obligation such as those contained in the clauses pleaded by Chevron eg 2.2, and 3.1.2(c).

41. No part of the clause deals with other types of costs or expenses that may be incurred by Chevron and, applying the general principle that there must be a clear expression of intention to limit liability, I do not consider that the contract expresses any such intention. Indeed, if one looks outside clause 3.4.3 the provisions of clause 9 in my judgment underline the parties' contemplation that Foster Wheeler may be liable for costs other than those immediately incurred by Foster Wheeler or Chevron since clause 9.4 and clause 9.8 deal with such costs. I refer to the section below where I consider clauses 9.4 and 9.8. I do not regard it as "inherently improbable" that Foster Wheeler should be held liable for those other losses e.g. Chevron's own engineering and other costs in investigating whether or not there was a breach, supervising the re-work, and any consequential costs including the cost of cleaning or purging or having tests carried out on other pieces of equipment not in themselves requiring rectification and their recommissioning. There is nothing in the clause or the contract which releases Foster Wheeler from its liability to pay Chevron for such costs. In my judgment it is inherently improbable that Foster Wheeler would not be liable for them since they are precisely the types of costs which, if they had been incurred by Foster Wheeler (and many of them might have been), would have had to have been borne by Foster Wheeler as part of the "expense". If therefore under the team work concept of this contract (even before Variation 14 added to

it) those costs or expense are wholly or partially incurred by Chevron in sharing the work to be carried out I see every reason why Foster Wheeler should remain liable for them and no reason why Foster Wheeler should be exempt from liability for them.

42. However if Chevron were to exercise the second option then in my judgment its rights under this clause are clearly limited to the "actual direct costs" even if these were in practice to mean that certain types of cost or expense were irrecoverable which might otherwise have been recoverable. The reason is plain: the scheme of clause 3.4.3 is primarily directed to enabling Chevron to obtain from Foster Wheeler the full physical benefits of its obligations under the contract. If Chevron elects to deprive Foster Wheeler of the opportunity to investigate a problem, to devise a solution and to execute it in such a way as not to affect the remainder of its work and services and thus Foster Wheeler loses control of the costs it does not seem to me to be unreasonable, particularly in this sector of the construction industry, for Chevron's rights to be limited. For example, it will not be able to recover costs that it has not actually incurred ie where it decides not to do what Foster Wheeler would have had to do. Foster Wheeler are similarly not to be accountable for costs which are not of a direct nature.

Clause 3.3.2

43. Clause 3.3.2(c) points ahead to clause 12 but it does not cover entirely the same ground as clause 12. (Again I consider this clause without regard to the effect of Variation 14.) In my judgment it creates considerable problems for Foster Wheeler's case for it imposes upon Foster Wheeler a duty not merely to examine the work or material provided by Chevron or others and to notify Chevron of any defect or discrepancy in that other work or material but also, if required by Chevron, to "correct such defect or discrepancy". Therefore, like the requirements of clause 3.4.3, Foster Wheeler may be under an obligation not merely to provide designs which overcome any defect or discrepancy (whether or not detected) but also, if the defect or discrepancy is not detected, and if the designs cannot be altered, to achieve the purposes of the contract by correcting the defect or discrepancy itself. In my judgment clause 3.3.2(c) fits in well with Mr White's submission that Foster Wheeler's obligations extend to ensuring that the Facility, when complete, will be suitable for its required and stated purposes.

44. Furthermore clause 3.3.2(c) has no express temporal limitation. Clearly the first paragraph is likely to bite during Phase II, although it may also apply during Phase III since there is no necessary reason why the obligation to inspect should not continue to be carried out as part of the "Follow-on Support Services" e.g. "supplying site query support; supplying engineering support at fabrication sites"; and "if requested providing testing and inspection assistance at manufacturers' works, at fabrication sites and off-shore". A site query may result in a drawing which had been otherwise approved for construction being corrected or updated or otherwise altered. Site queries are likely to originate from Chevron or its contractors but there is no necessary reason why they should not originate from Foster Wheeler. The teamwork concept does not stop with Phase II so it would be odd if the operation of clause 3.3.2(c), first paragraph, should cease at the end of Phase II.

45. If therefore in the course of carrying out the "dependent work" the defect or discrepancy is discovered then Chevron "may reject such defective or discrepant work or material". Obviously it need not do so since it might instead decide to require Foster Wheeler to put right an offending design if that would obviate the correction of the "discrepant work". There is no obligation on the part of Chevron to require Foster Wheeler to put right the discrepant work. Chevron may put right the discrepant work itself (but if it does so Foster Wheeler can still contend that it was unreasonable to have done so under ordinary principles of mitigation.) In such circumstances there is nothing in clause 3.3.2.(c) and none elsewhere, which would exclude or limit Foster Wheeler's liability for a defect of the kind described in clause 3.3.2(c), if it were a breach of contract.

46. It was suggested, however, that the reference forward to clause 12 in some way limited Foster Wheeler's liability. I disagree. The part of clause 3.3.2(c) which refers to clause 12 is merely a signpost or pointer to the clause which will deal with what is to happen if Chevron were to exercise its right to require Foster Wheeler to put right the defective or discrepant work or materials. Clause 12.1 does no more than state that if Foster Wheeler were required to put right work that had been rejected then it must do so "as soon as practicable after receiving notice thereof from COMPANY" and "at CONTRACTOR's expense". So there is in my judgment no obvious limitation on Foster Wheeler's liability under clause 3.3.2(c). Reading clause 3.3.2(c) with clause 12 it is clear that a defect requiring correction under 3.3.2(c) will lead to Chevron suffering loss or damage if Foster Wheeler do not put it right. The contract therefore treats this class of defect (if it appeared prior to Acceptance) as more than a "temporary disconformity" and as a breach of contract. In my judgment there is no clearly expressed intention in clause 3.3.2(c) that Chevron is not to recover any loss or damage otherwise recoverable in law and resulting from a failure by Foster Wheeler to put right the defective or discrepant work, whether pre- or post-Acceptance. Thus clause 3.3.2(c) does not afford Foster Wheeler with protection from such a claim. If on the other hand Foster Wheeler acts to put right the work when required by Chevron then clause 3.3.2(c) in stating that the corrective work is carried out "on the basis set forth in Section 12 hereof" means that Chevron's rights and any limitations on Foster Wheeler's liability are to be found in that Section, to which I now turn.

47. Mr Reese QC advanced an attractive argument to the effect that clause 12, in the context of the contract of the whole and in particular clause 3.4.3, clearly provides that
    1. prior to Acceptance Chevron could require Foster Wheeler to re-work its design;
    2. after Acceptance, the remedies available to Chevron are limited to those set out in the guarantee in Section 3 (clause 3.4.3);
    3. prior to Acceptance Chevron should be in no better a position.

(The reference in clause 12.1 to "the guarantees stated in Section 3.3.2" must be a numbering error as the guarantees are found in clause 3.4.3; a literal interpretation would also lead to circuity.)

48. It is clear that the last sentence of clause 12.1 simply summarises the position under clause 3.4.3. The words "shall be replaced or reperformed" read in conjunction with the previous requirement that prior to Acceptance the contractor is to replace and reperform the defective work import an obligation on the part of the Contractor and assume that the first option in clause 3.4.3 will be chosen by Chevron. This must therefore be regarded as the normal contractual route for the rectification of defective work. If Chevron elects to take the second route the extent of Foster Wheeler's liability for defects appearing after Acceptance may not be the same so, as I have set out in my conclusions on clause 3.4.3, Foster Wheeler's position will depend on what Chevron decides and does. Clause 12 does not affect those conclusions, as it simply refers the reader to clause 3.4.3 to find out what is to happen post Acceptance.

49. Similarly the general wording of the first part of clause 12.1 applies to all defects appearing prior to Acceptance and thus comprehends Foster Wheeler's obligations under clause 3.3.2(c). There is no express limitation of liability in clause 12.1 but Mr Reese argued that it would be wholly unreasonable and inconsistent with the plain intention of the contractual code if Foster Wheeler were liable for loss and damage suffered by Chevron consequent on the discovery of a defect which Foster Wheeler were then required to and did make good. The most obvious instance was the correction of an error in a proposed design since the contract envisaged that the process of working together and the procedures of scrutiny and approval would not necessarily prevent such an error and thus the scope of the work in Exhibit III included "(e) Correcting and updating all drawings approved for construction to "as built" condition; (f) Correcting and updating all construction drawings to "as built" condition". Such corrections might also be required for other reasons. Foster Wheeler's case was that since the correction of errors was expressly provided for in the contract without any provision being made for Chevron to recover any costs that it might have incurred in consequence, the risk of loss due to errors occurring during the course of the project was plainly to be borne by Chevron. The words "at CONTRACTOR's expense" in clause 12.1 showed that Foster Wheeler were only to bear its own costs.

50. Mr Reese submitted that it would be unrealistic if Foster Wheeler were to pay Chevron in effect for its costs of supervision, scrutiny and approval.

51. Mr White maintained that the requisite clarity of language was not to be found; that clause 3.4.1(d) and 3.4.2(c) preserved Chevron's rights; and that such rights included the right to receive damages in lieu of the performance of the primary obligation.

52. I consider that the scheme of the contract makes it clear that the likelihood of a claim for significant damages for breach of contract arising prior to Acceptance is low. First, if arrangements were made as outlined in Exhibit II then mistakes made by Foster Wheeler in the preparation of the detailed design of the engineering work and in the production of the relevant documents ought normally to be picked up either in the course of working together as a team or by Chevron in the course of formal scrutiny and approval. If these procedures do not operate as intended e.g., if, as sometimes happens when these arrangements are made, Foster Wheeler were to carry out its work in a less than satisfactory manner leaving Chevron to incur inordinate time and cost in scrutinising the work proffered, in pointing out mistakes, and in returning the work for re-submission before it can be approved, then (quite apart from clause 9.4(b)) there would be less reason to exempt the contractor from its responsibility to pay compensation for what would then be a clear breach of its obligation to carry out its part of the contract "with due diligence and in accordance with generally accepted, current good practice of the industry and trades involved". Even so, not every such mistake need be a breach of contract for the scheme of the contract plainly envisages that Chevron may pick up mistakes and get the drawings amended by Foster Wheeler before approval, and that its costs of so doing would be borne by it within the intention of the basic contract framework. Foster Wheeler is not required to be perfect during the course of any Phase. Therefore whether Foster Wheeler is in breach of its obligations will be a matter of fact (was a mistake in fact made?) and degree (is such a mistake or series of mistakes beyond that to be tolerated under the contract?). If the answers to these questions are both: Yes, then Foster Wheeler is likely to be in breach of contract. These questions do not of course arise for determination now.

53. Foster Wheeler's case does not satisfactorily resolve what is to happen if there is a major error leading to substantial losses. Clause 9 makes it clear that there is a wide ambit of loss for which Foster Wheeler will be liable. I do not consider that the fact that the contract expressly provides what is normally to happen (ie Foster Wheeler is to put rights defects at its own expense) leads to the inference that Foster Wheeler is not liable for losses which Chevron may suffer. In my judgment the likelihood that such losses will arise only rarely is a reason to look for a clear expression of limitation but it is not to be found in clause 12.1, although it is found in clause 9.4(b). In my judgment the contract strikes a not unreasonable balance. Each party is given the basic commercial protection which they may be expected to desire: Foster Wheeler should not normally have to pay Chevron's costs arising out of day-to-day errors that will inevitably arise on a complex project because either they will not be breaches of contract or Chevron must be taken to have allowed for them; Chevron, on the other hand, will not be deprived of its inherent right to claim damages for breaches of contract. If Foster Wheeler were not to comply with its obligations under clause 12.1 to put right a defect there are no grounds for limiting the extent of its liability (apart from the application of clause 9.4(a) and (b) and clause 9.8) and I see no logical reason why Chevron's right to recover losses which it may incur (irrespective of whether the defect is put right by Foster

Wheeler or by Chevron) should depend upon whether Foster Wheeler complies with its obligation under clause 12.1.

54. Whilst therefore there might appear to be a distinction between Foster Wheeler's exposure prior to acceptance and that following acceptance under clause 3.4.3, I do not consider that, on analysis, there is likely to be such a distinction in practice. Any difference is likely to be to be due to Chevron's own decisions and actions. Moreover since the contract envisages that Foster Wheeler is to be given the opportunity of putting right its errors (by correcting designs or by remedial work) then, as I have previously stated, Chevron may have to justify a decision not to utilise its contractual remedy especially if any of its expenditure would have been avoided had Foster Wheeler been required to act.

Clauses 9.4 and 9.8

55. Foster Wheeler placed reliance upon these clauses as indicative of the overall frame work of the contract. In approaching these clauses I bear in mind that they form part of a group within Section 9 which is primarily concerned with the distribution of liability for and the effect on others of any negligence or breach of contract on the part of Chevron or Foster Wheeler. The provisions of Section 9 are clearly a prelude to the requirements of Section 10 which set out Foster Wheeler's obligations as to insurance. Clauses 9.1 and 9.2 deal with personal injury and death of employees of Foster Wheeler or its sub-contractors and Chevron. Clause 9.3 deals with loss and damage to property of Foster Wheeler or its sub-contractors (to its sites, facilities, motor vehicles, aircraft and buildings and contents etc). (Clauses 10.1, and 10.2, and 10.3 all commence with words indicate that they are not intended to limit Foster Wheeler's liability under Section 9 and accordingly no reference was or should have been made to them as a means of determining the ambit of the clauses in Section 9.)

56. Clause 9.4 (a) (which is applicable both before and after Variation 14) is concerned with "loss, damage or destruction of any property of the Group (including the Facility)". The clause is notable in a number of respects. It begins by restating Foster Wheeler's obligations: *"CONTRACTOR shall exercise due care and diligence in the performance of this Agreement and in the design of the Facility and CONTRACTOR shall be liable for and shall indemnify the Group against losses, damages, compensation, claims, demands, proceedings, costs, charges and expenses in respect of each event of loss, damage or destruction of any property of the Group (including the Facility), caused by or arising out of*

57. The first limb of the clause is strictly unnecessary except to underline that the second limb contains two objectives: a provision that the contractor shall be liable and a provision that the contractor shall indemnify.

58. Clause 9.4 concludes by stating that Foster Wheeler "shall have no such liability" unless notice has been given and within certain periods. Although it was suggested that the effect of the inclusion of an obligation to indemnify has the effect of extending the limitation period, I doubt if in this instance it would have that effect since the words "no such liability" refer to "liability hereunder" and thus include the liability arising from the obligation to indemnify. There is a further limitation placing a ceiling of £1 million in respect of any one event. The clause also makes Foster Wheeler liable "regardless of negligence and any other liability of [Chevron]".

59. Foster Wheeler's liability under clause 9.4 may extend to the Group and may also be extended further by virtue of clause 28, so that companies other than Chevron may recover their losses: see also the Recital and Definitions clause 1.1(p). As a result of the additional obligation to indemnify the scope of Foster Wheeler's liability is therefore somewhat greater than it would be towards Chevron alone for breach of contract. This does not suggest any inherent limitation on Foster Wheeler's liability but rather the commercial one, perhaps linked to insurance cover, of limiting the extent of the remedy available, particularly where, as here, Foster Wheeler's liability extends beyond the immediate contracting party of Chevron.

60. What is important to the determination of Issue 3 is the clear limitation of liability to be found in clause 9.4 (both before and after Variation 14). This clear expression of intention is therefore to be contrasted with the language used in the other clauses upon which Foster Wheeler rely and in my judgment lead to the inescapable conclusion that the only limitations which satisfy the applicable principles of law are those to be found in the fifth paragraph of clause 3.4.3 and in Section 9. That is not to say that the contract does not contain a code for regulating what is to happen if a defect is found. Obviously clause 9.4, like clause 3.4.3 and, to an extent, clause 3.3.2(c) and clause 12, commences with a re-statement of Foster Wheeler's primary obligations, and then sets out the extent of Foster Wheeler's secondary obligations, but it does not in my view follow that the statements of Foster Wheeler's immediate practical obligations in clauses 3.3.2(c) (by reference to clause 12), 3.4.3, and 12 must also be regarded as a comprehensive and exhaustive re-statement of Foster Wheeler's secondary obligations, and of the limited remedies available to Chevron. With the exception of the fifth paragraph of clause 3.4.3 none of the clauses deal with the totality of Foster Wheeler's legal responsibilities. The contractual framework has some similarity to that in ***Hancock v B.W. Brazier (Anerley) Ltd*** [1966] 1 WLR 1317 in which Diplock LJ, whose decision at first instance was affirmed, said at page 1328:

> *"I can see no reason why, because an alternative remedy is given for a limited number of breaches of a limited kind discovered in a limited period, I should hold that by some implication the plaintiffs have given up all rights which clause 9 expressly bestows upon them."*

61. Clause 9.7 deals specifically with pollution or contamination and appears to be declaratory of an extended obligation rather than of an existing one. Clause 9.8 is typical of its kind insofar as it limits liability for certain heads of loss or expense that might otherwise be recoverable as damages for breach of contract namely "any

loss of contract, product, production or profit, business interruption and similar form of consequential damage...". It is however a clause that applies equally to both Foster Wheeler and its sub-contractors and to Chevron. I am not asked to decide on the extent to which the clause might apply to the circumstances assumed to be typical of Chevron's claims in this case. There is plainly a limitation on Foster Wheeler's liability but whether clause 9.8 has any impact must depend upon proof of Chevron's case.

62. Accordingly for these reasons Issue 3 will be answered:

No, unless the circumstances fall within the fifth paragraph of clause 3.4.3, and subject to the overall limitations set out in Section 9.

Issue 2 Whether it was an implied term of the contract that reimbursable costs would be reasonably and properly incurred?

63. This issue raised a consideration of the following clauses in addition to some of those to which I have already referred:

"1.1 (l) "direct costs" whether payable by COMPANY to CONTRACTOR or by CONTRACTOR to COMPANY means substantiated direct costs.

(x) "Reimbursable Cost" means those costs incurred by CONTRACTOR and indicated as being reimbursable in Exhibit II - Basis of Compensation.

(dd) "wage costs" means the wages actually paid to the CONTRACTOR'S personnel and all costs to CONTRACTOR (i) for any and all taxes, contributions or assessments for unemployment insurance required by law which are measured by or based upon said wages including contributions or assessments for Workmen's Compensation or Industrial Injury Benefit and premium for insurance against the aforesaid and (ii) for all benefits to be paid to or on behalf of the CONTRACTOR's personnel, such as reimbursement for transportation, subsistence, health and welfare, pension, vacation, holiday, training and other funds which CONTRACTOR is required to pay in accordance with governmental regulations or collective agreements with recognised trade unions with membership in the specific area of the Work hereunder.

6.1 CONTRACTOR's total remuneration for the performance of all of its obligations pursuant to this Agreement shall be the sum of the amounts determined by the Basis of Compensation in Exhibit II hereof.

6.2 <u>ADJUSTMENTS TO REMUNERATION</u>

CONTRACTOR's remuneration shall not be changed on account of any change in conditions affecting the Work, or on account of any other difference between the anticipated and the actual performance of this Agreement, or for any other reason except as follows:
(a) COMPANY requires a Variation pursuant to Section 2.5 hereof.
(b) COMPANY directs and CONTRACTOR takes acceleration measures pursuant to Section 8.3 hereof.
(c) CONTRACTOR's reimbursement shall be increased by the total of the reasonable direct audited costs necessarily incurred by CONTRACTOR due to COMPANY caused delays or suspensions as provided in Section 8.4 hereof unless CONTRACTOR is also in default.

<u>SECTION 7 - COMPENSATION, INVOICING AND PAYMENT</u> ....

7.2.1 <u>Reimbursable Costs and Supporting Detail</u>

(a) CONTRACTOR shall submit to COMPANY at the end of each calendar month during the progress of the Work hereunder, a Reimbursable Costs invoice for costs incurred in such calendar month. Such invoice shall be submitted in duplicate and shall:
(iv) be accompanied by one copy of details to support an audit of CONTRACTOR's charges, including the name, classification, rate and time (supported by a signed time sheet) worked by each individual, expense accounts ...., statements, receipts and invoices,....and specific details on all other Reimbursable Costs, all of which shall be in a form acceptable to COMPANY.

7.3 <u>Payments</u>

7.3.1 Subject to the provisions of Section 16 and Section 20 of this Agreement and Subsection 7.3.3 below, COMPANY will pay CONTRACTOR the amount payable within thirty (30) days after receiving CONTRACTOR's invoice. PROVIDED always that the provision by CONTRACTOR of the insurance required by Section 10 hereof and the provision of certificates or renewal certificates to evidence such insurance shall be a condition precedent to COMPANY's payment of any of CONTRACTOR's invoices.

7.3.3 COMPANY shall have the right to deduct from any payments to CONTRACTOR any amount which COMPANY is required to deduct by any Act of Parliament, statutory instrument or other law or regulation which is applicable to this Agreement hereto and to pay any deducted amount to the party and in the manner provided therein. Further, COMPANY shall have the right to deduct from any payments to CONTRACTOR, or suspend in whole or in part, payments to CONTRACTOR whilst CONTRACTOR is in Default pursuant to the Agreement.

7.3.4 If COMPANY shall dispute any items of an invoice in whole or in part, COMPANY shall not delay payment of the undisputed part of the invoice provided that in such event CONTRACTOR shall, before COMPANY is required to make any payment, furnish COMPANY with a credit note for the amount of such invoice which COMPANY disputes and such credit note shall include Value Added Tax, if any is chargeable, on such

disputed amount and provided that the thirty day payment period referred to above shall be suspended at the time that COMPANY notifies CONTRACTOR of such dispute and shall recommence on the date that COMPANY receives CONTRACTOR's credit note. The issuing of a credit note by CONTRACTOR shall not itself in any way be evidence of acceptance by CONTRACTOR that COMPANY is correct in disputing that part of the invoice to which the credit note relates.

16.4 CONTRACTOR shall assist COMPANY in making the above audit.

EXHIBIT I

3.1 ***Project Support Services Support***

Provide all required support and input to the Project Support Services Group for the control, recording and reporting of planning, progress, design and materials/equipment vendor documentation, weight control, design change control and design manhours/cost control. QA and QC document control, and such other aspects of the Work as COMPANY may request.

Pursuant to the requirements of Subsection 6.1 COMPANY shall pay CONTRACTOR a total compensation in accordance with the provisions of this Exhibit II. Provided always that CONTRACTOR shall perform and observe its obligations under the Agreement and such total compensation shall be deemed to be CONTRACTOR's complete entitlement under the Agreement.

1.2 ***Firm Price***

Except as otherwise expressly stated herein the rates and prices stated in this Exhibit II shall be fixed and not subject to variation in the period to 31 December 1991."

64. Section 2 dealt with "Compensation". It stated (1) that the rates contained in Schedule A were to be used to compensate Foster Wheeler for the "direct costs of personnel for all work carried out during Phase I and, if so authorised Phase II and if so authorised, such work as is undertaken at the contractor's home office during the follow-on support services"; (2) that the rates contained in Schedule B shall be used to compensate Foster Wheeler "for all Work, if so authorised, carried out at a Fabrication Site or Offshore during the design phases or Phase III; (3) that the rates contained in Schedule C should be used to pay Foster Wheeler for the provision of office accommodation; (4) that the rates in Schedule D were to be used for technical computer services; and (5) that the rates contained in Schedules E and F were to be used for other purposes.

65. Exhibit II (unamended by Variation 02) continued as follows:-

2.2.1 The rates contained in Schedule A unless expressly stated otherwise are deemed to include the following:-

(a) All costs of employment of CONTRACTOR's direct, indirect, productive and non-productive labour, including all associated costs, direct remuneration, payroll related expenses and other direct and indirect costs and expenses.

(b) All sub-contract administration.

(c) All non productive time.

(d) All necessary consumable items.

(e) All insurance and associated costs.

2.2.2 The Weekday Overtime and Saturday/Sunday Working rates contained in Schedule A unless expressly stated otherwise are deemed to include for all items pursuant to item 2.2.1.

2.2.3 The rates set out in Subsection 2.2.1 and 2.2.2 above are fixed until 31st January 1991. Thereafter at COMPANY's sole discretion the salary and payroll burden portion of the rates amy be adjusted based on the average salary or contract rate variation for each grade. Such variations will be reviewed with reference to local market trends. Subsequently rates may be reviewed quarterly."

66. The schedules set out the labour rates and defined what would be the normal time for which the rates would be payable in the case of labour. The same policy was continued by Variation 02. The rates were firm and inclusive of non-productive time and incidental and ancillary costs. The inclusion of factors such as non-productive time clearly do not help Chevron to mount a challenge to the hours worked and the details of the components indicate Chevron might have provided expressly for what it now contends is obviously and reasonably to be implied. Similarly, Exhibit III provided for a "Incentive Programme". Paragraph 3 of that Exhibit was headed "Progress Incentive" and stated as follows:-

"3. ***Progress Incentive***

Subject to satisfactory performance in the opinion of the Programme Evaluation team the CONTRACTOR will be paid the management fee rate per hour for each direct manhour saved in the achievement of any CTR workscope.

This additional payment will not be made in event that:

a) The standard of work produced fails to meet the standards required by COMPANY.

b) The CTR workscope is not completed within the times agreed and set out in the project agreed between CONTRACTOR and COMPANY from time to time.

In the event that on any CTR workscope, the CONTRACTOR expends manhours in excess of those agreed by the programme evaluation team then the management fee relating to such additional manhours will not be payable to CONTRACTOR.

For the purpose of calculation of progress incentives each CTR workscope activity shall be treated as an independent workscope.

4. ***Innovation***

If after the agreement of a CTR workscope CONTRACTOR in the progress of its workscope require [sic] to spend additional time in design of new areas of technology or where a fundamental change in design philosophy occurs or in order to pursue aspects of design which will provide an improved balance of first cost versus operating and maintenance cost then CONTRACTOR may subject to the provisions of clause 2.5 of the Agreement propose that the CTR manhours allowed for such a workscope are amended.

Should COMPANY agree with such a proposal and consider that further investigation/design is required then at its sole option COMPANY may authorise the programme evaluation team to increase the manhour target on the particular CTR workscope.

The application of the Progress Incentive, will then be applied to the revised CTR manhour estimates."

67. I have already referred to Exhibit IV which set out the project organisation and the arrangements for the parties to work together (prior to Variation 14).

68. During the course of argument Mr White accepted that both Issue 2 and the implied term set out in Paragraph 11 of the Defence and Counterclaim were not precisely formulated since they referred to reimbursable "costs" whereas, as appears from Exhibit II, Foster Wheeler's remuneration was to be calculated by the application of agreed rates to hours worked. The real question is whether Chevron could question whether the hours worked had been reasonably and properly incurred.

69. Foster Wheeler's case was that the contract dealt with the question of the hours worked in express terms (as indeed it did with certain aspects of verification of the hours themselves) and under ordinary principles there was no reason to imply the term. Reference was made to well known cases such as ***BP Refinery (Westernport) Pty Limited v. Shire of Hastings*** (1978) 52 AJLR 20; ***Liverpool City Corporation v. Irwin*** [1977] AC 239, and in the context of the court's unwillingness to imply terms where the express terms leave no room for them: ***Martin Grant & Co Ltd v Sir Lindsay Parkinson & Co Ltd*** (1984) 29 BLR 31.

70. Mr White argued that the term was necessary and reasonable and did not conflict with any express term of the contract and was required because otherwise Chevron would have no means of avoiding payment for hours expended in the preparation of designs and in the execution of work which subsequently proved to be defective, particularly in the context of the re-work claims, and in the time spent in putting right those defects. Chevron were not to find themselves obliged to pay Foster Wheeler both for doing the original work defectively and for putting right the defects. Stated in that way the term has much to commend it. However, Mr Reese QC argued that the parties had entered into an agreement which had been carefully drawn up and, essentially, if Chevron had wanted that right in addition to all their other rights and provisions in the contract, they could and should have so stipulated. It was therefore not a term to be implied.

71. In order to determine the strength of Foster Wheeler's argument it is necessary to examine the revisions of the contract. Mr White drew attention to the structure of the contract as set out in Exhibit II and III whereby the work was split into workscopes or Segments each with its own CTRs. Whatever may have happened in practice - and it appears that the scheme may not have been implemented as envisaged - at the date of contract the parties envisaged that there was to be agreement on the CTRs before the next Phase was authorised. Those for Phase I would have been agreed as part of the agreement of the original contract; those for Phases II and III would have to be agreed for otherwise Foster Wheeler would not be awarded either Phase II or for Phase III, respectively. Nevertheless Mr White pointed out that even if the hours were agreed there was no means whereby Chevron could avoid paying for the hours if they were unproductively employed.

72. It seems to me that there are two fundamental flaws in Mr White's case.

73. First, Chevron has rights to audit Foster Wheeler's books to see whether Foster Wheeler could prove that the hours for which they claimed and which they were due to be reimbursed had in fact been worked. I agree with the submission of Mr Reese QC that clauses 7.2.1(a)(iv) and 16.3 of the contract are directed to what might be called an "accountancy" audit rather than a "engineering" audit since it is plainly linked to clause 16.5 and other provisions of the contract e.g. those in Exhibit II. Clause 16.3 is expressly limited in its scope as the last sentence precludes the audit of "items of remuneration such as fixed rates, fixed percentages or fixed lump sums." The records which the contractor is required to keep under clause 16.1 are those referred to in clause 4.2 which states:

"CONTRACTOR shall maintain adequate accounting records during the progress of the Work for cost control purposes to provide the basis for CONTRACTOR's remuneration hereunder pursuant to Section 6 of this Agreement and for the purpose of Audit pursuant to Section 16 of this Agreement. ...."

74. Clause 7.2.1(a)(iv) is also relevant since it refers to "details to support an audit". These provisions clearly show that the parties directed their minds to the checks that Chevron would be entitled to carry out and confined them

to verification of matters such as the actual hours claimed to have been worked by Foster Wheeler, the names and grades of those engaged, and the amounts of expenses etc claimed. There is no reference in any clause to any requirement to keep records of the nature of the work done so that Chevron could verify whether the hours were reasonably and productively spent.

75. Secondly, if the audit were to disclose that there had been an overpayment then Foster Wheeler were obliged promptly to reimburse the amount overpaid - see clause 16.5(d) (for subcontractors) and clause 7.3.4 which requires Foster Wheeler to give Chevron a credit note where Chevron disputes an invoice where Chevron consider there has been an error of fact:

"These provisions shall apply equally in the case of errors of fact including errors in arithmetic, except that when, in the opinion of COMPANY, an invoice is manifestly and substantially wrong, COMPANY may return the invoice to CONTRACTOR with the request that it be resubmitted in correct form."

and the more general provisions of clause 7.3.5:-

"COMPANY shall be entitled to recover at any time overpayments which have been made to CONTRACTOR."

76. Clause 7.3.3 also confers express powers of deduction and withholding where Foster Wheeler has been in default. There are therefore express provisions of the contract relating to the mechanics of repayment.

77. Thirdly, Exhibit III made provision for incentives and thus itself expressly provided a mechanism whereby Foster Wheeler could earn more by way of a bonus paid via the management fee rate (see paragraph 3) in the event that they achieved the work required in less time than that contemplated by the agreed CTR. The paragraph states that if Foster Wheeler spends more time than that allowed in the CTR then the management fee would not be payable in relation to the excess hours.

78. In my judgment it is plain that there is no room for the implication of a term as suggested by Chevron. If as Mr White suggested the contract has manifest inadequacies which need to be made good by such a term then Chevron could and should have added to the already extensive repertory of remedies available to it. Work could not be carried out without prior agreement as to CTRs. Chevron had then the opportunity to define what would be the reasonable and proper time required for each workscope or subject matter of a CTR that would be acceptable to it. If Foster Wheeler thereafter did better than the hours in a CTR Chevron would pay for fewer hours than contemplated and would pay Foster Wheeler a bonus by way of an enhanced management fee. If Foster Wheeler overran then it would lose its management fee but Chevron did not stipulate for any other remedy and agreed to pay for the time actually spent, no doubt because the loss of a management fee was thought to be sufficient to ensure that the hours were productively employed. The implied term therefore covers ground already the subject of express terms (see **Martin Grant**) and conflicts with the detailed contractual scheme or repertory and is in any event unnecessary to give business efficacy to a contract which must be treated as one which has been carefully negotiated.

79. Finally, if some workscope or definable work were to be carried out without due diligence and thus contrary to clause 2.2 and if as a result Chevron had paid or might be required to pay for time spent in breach of contract then it could recover those amounts as its damages. But, as I have already indicated, such a claim would have to be one justified both in fact and degree taking into account the valid point that work is not carried out to perfection and to the utmost expedition on every occasion. If that hurdle could be overcome Mr White was right in his submission that Chevron would be able to rely on the well-known principle which was restated in ***Alghussein Establishment -v- Eton College*** [1988] 1 WLR 587 [2] in which Lord Jauncey of Tulleychettle said at page 594:

"Although the authorities to which I have already referred involved cases of avoidments a clear theme running through them is that no man can take advantage of his own wrong. There was nothing in any of them to suggest the foregoing proposition was limited to cases where the parties in breach were seeking to avoid the contract and I can see no reason for so limiting it. A party who seeks to obtain a benefit under a continuing contract is just as much taking advantage of his own wrong as a party who relies on his breach to avoid a contract and thereby escape his obligations".

Issue 2 will therefore be answered: No

Issue 1 (a) Whether the defendant has right at common law to set off damages sustained by it as a consequence of breaches of contract on the part of the plaintiff?

80. The scope of this issue was reduced in so far as Mr Reese QC for Foster Wheeler conceded that if Foster Wheeler were held to be in breach of the contract and if Foster Wheeler were thereby liable for some loss or damage which was recoverable under the terms of the Contract then Chevron might set off such loss and damage against sums otherwise due to Foster Wheeler. Mr Reese QC did not however concede that there was any general right to set off damages for breach of contract. There is therefore little to decide since Mr Reese QC's concession appears effectively to answer the issue, especially since the terms of a contract include implied terms. In any event the point can be dealt with quite shortly. Mr White relied upon ***Modern Engineering v. Gilbert-Ash*** [1974] AC 694 per Lord Diplock at 718E (which has already been quoted):-

[2] See also ***CIA Bareada Panama SA -v- George Wimpey & Co Ltd*** [1980] 1 Lloyd's Rep 598 per Bridge LJ at page 609. col 1. where he set out a "succinct statement of principle" from Williston on Contract: *"It is a principle of fundamental justice that if a promisor is himself the cause of the failure of performance either of an obligation due him or of a condition upon which his own liability depends he cannot take advantage of the failure."*

"So when one is concerned with a building contract one starts with the proposition that each party is to be entitled to all those remedies for its breach as would arise by operation of law, including the remedy of setting-up a breach of warranty in diminution or extinction of the price of materials supplied or work executed under the contract. To rebut that presumption one must be able to find in the contract clear unequivocal words in which the parties have expressed their agreement that this remedy shall not be available in respect of breaches of that particular contract."

81. Mr White submitted that there were no clear unequivocal words in this contract. It is clear from the decision of the House of Lords in ***Mottram Consultants Ltd v. Bernard Sunley and Sons Ltd*** [1975] 2 Lloyd's Rep 197 that the words need not be explicit, provided that they are clear. However, I find nothing in the contract which would prevent Chevron raising as an equitable set-off a claim for damages for breach of the contract which is not preserved by the express terms of the contract. Indeed the provisions to which I have referred relating to overpayments and their recovery appear to me to be entirely consistent with the intention to be inferred from the contract that Chevron should be entitled to recover from Foster Wheeler amounts to which Foster Wheeler were not entitled and are not to be read as limited to those rights. Such a conclusion does not of course mean that the claims which Chevron seek to maintain by way of set-off are correctly so maintainable. It may well be the case that Chevron's rights in relation to, for example, overpayments, are those governed by the express terms of the contract to which I have referred. But a decision on the specific claims and whether they fall within Chevron's preserved right at common law to set-off damage sustained by it as a consequence of a breach of contract on the part of Foster Wheeler, must await the outcome of the trial itself.

This sub-issue will therefore be answered: Yes.

Issue 1(b) Whether the defence of abatement is excluded by the Contract.

82. As Chevron can advance an equitable set-off against Foster Wheeler's claims, this issue is in practical terms even narrower than Issue 1(a), although as Ralph Gibson LJ said in ***Acsim (Southern) Ltd v Danish Contracting etc Ltd*** (1989) 47 BLR 55 at page 71 the defence of abatement does not necessarily raise a breach of contract and may consist merely of asserting that the sum claimed has not been earned. For the reasons already given the defence of abatement is not excluded by the terms of the contract, if only because the provisions as to recovery of overpayments based upon errors of fact reinforce the presumption that the parties intended to retain their rights at law. The issue does however give rise to an interesting point.

83. Mr Reese QC and Mr Lofthouse argued that the defence of abatement was not open to Chevron as the contract was one for professional services, and that the defence of abatement was not available for such contracts. For the latter proposition they relied principally upon ***Hutchinson v. Harris*** (1978) 10 BLR 19. In that case a claim had been made against the defendant architect for negligence. One of the issues on the appeal was whether the architect's counterclaim for the balance of her fees could be applied as a cross-claim to reduce the amount of the plaintiff's claim. For the plaintiff it was argued that the counterclaim for fees ought to have been abated on account of the claim for negligence. Stephenson LJ considered the contract between the architect and her client (see 10 BLR 30-31), in the course of which he expressed reservations about whether "professional work and labour" was a correct description of the architect's services, and then said, at page 31:-

*"That leads to another point, and that is how far this head of defence which can be set up in abatement of price can be applied to a claim for professional services. That is, of course, in a sense a claim for work and labour done, but it is clear, from the language of the learned Baron which I have read [Parke B in **Mondel v. Steel** (1841) 8 M and W 848] that what he had in mind was a specific chattel like a ship, which might be bought or upon which work and labour might be done. I find the greatest difficulty in applying this defence of abatement to a claim for professional services, certainly to such a claim for professional services as we have here. And it is not without interest that neither counsel has been able to call our attention to any case, reported or unreported, with one possible exception, in which such a claim for professional services has been reduced or abated by the application of **Mondel v. Steel**. The nearest, perhaps, we get to it is the case of **Hoenig v. Isaacs** [1952] 2 All ER 176, where the plaintiff claiming the cost of work and labour was an interior decorator or a craftsman and not a professional person like a surgeon or a solicitor. It is also not without interest that in **Mondel v. Steel** the Court did refer to a case of an attorney, **Templer v. M'Lachlan** (2 Bos & Pul 936; 127 ER 576), of which Parke B said:-*

*"The same practice has not, however, extended to all cases of work and labour, as, for instance, that of an attorney, **Templer v. M'Lachlan**, unless no benefit whatever has been derived from it."*

I do not refer in detail to that case. It was decided by reference to reasons, some of which might no longer hold good today. But there is no case, which has been cited to us, in which somebody in the position of an architect has had his or her claim for fees abated under this doctrine, except possibly the case to which I must now refer; and, as I say, I see the greatest difficulty in replying the doctrine to such a claim as is made by way of a counterclaim here."

84. Stephenson LJ then referred to ***Sincock v. Bangs (Reading)*** [1952] JPL 562 which he doubted.

85. Mr Reese QC also relied upon ***Cathery v. Lithodomos Ltd*** (1987) 41 BLR 76. That was an appeal against an order refusing an application that the defendant should give security for the cost of a counterclaim. The plaintiff was a consulting engineer who had been engaged by the defendant developers and building contractors and who brought the action to recover for additional fees. By its counterclaim the defendant alleged that the plaintiff had been negligent and claimed damages. The defendant relied upon the counterclaim as an equitable set-off to

extinguish the plaintiff's claim. Dillon LJ at page 82, said that there was no doubt that the counterclaim could properly be treated as an equitable set-off and then said:-

"The defendants do not put forward any defence of abatement such as might be pleaded at common law in an action for the price of goods sold or the cost of work and labour, viz that the goods or work were not up to standard required by the contract and so the price should be reduced. That is not pleaded since it was held in ***Hutchinson v. Harris*** (1978) 10 BLR 19, by this Court that such a defence is not available to a defendant in an action by a professional firm for fees. In such an action the proper course is for the defendant to counterclaim for damages for professional negligence and breach of duty on the part of the plaintiffs and plead an equitable set-off."

86. Mr Reese QC accepted that there was no rational justification for the position that the defence of abatement is not available against a claim for the value of professional services but submitted that the law was as stated by Stephenson LJ in ***Hutchinson v Harris.*** It is indeed hard to see why a defence which is available to a contract for work and labour is not available in a contract for professional services. The distinction based on the nature of the product of the performance is not persuasive, as drawings or a specification or a document, may be valueless or of less value if improperly prepared just as any other chattel. **Wood on International Set-off** says at paragraph 4-35:

"*The placing of a fence around contracts for the sale of goods or for work and labour seems curiously arbitrary*".

Nevertheless the weight of opinion in the Court of Appeal cited to me makes it clear that that is the law which I must apply.[3]

87. Mr White however challenged the submission that the contract between Foster Wheeler and Chevron was one for professional services and therefore not one to which the doctrine of abatement could apply. He submitted that the contract was one for work and labour. He relied first upon ***Robinson v. Graves*** [1935] 1 KB 579. The plaintiff was a portrait painter who had been commissioned on 27 July 1932 by the defendant to paint a portrait of Miss Finnegan for a fee of 250 guas. She attended one sitting but on 2 August 1932 the defendant repudiated the contract.[4] He defended the action for the fee (inter alia) on the grounds that the contract was oral and therefore unenforceable as it was a contract for the sale of goods for which a note or memorandum in writing was required, as provided by section 4 of the Sale of Goods Act 1893. The plaintiff maintained that the contract was one for work and labour. Acton J. rejected that submission but otherwise found for the artist whose appeal was successful allowed. Greer LJ said at page 584:-

"Looking at the propositions involved from the point of view of interpreting the words in the English language it seems to me that the painting of a portrait in these circumstances would not, in the ordinary use of the English language, be deemed to be the purchase and sale of that which is produced by the artist. It would, on the contrary, be held to be an undertaking by the artist to exercise such skill as he was possessed of in order to produce for reward a thing which would ultimately have to be accepted by the client. If that is, the contract in this case was not a contract for the sale of goods within the meaning of s. 4 of the Sale of Goods Act, 1893."

Greer LJ then considered the authorities and concluded (at page 587):-

"If you find, as they did in ***Lee v. Griffin*** *(1861) 1 B & S 272, that the substance of the contract was the production of something to be sold by the dentist to the dentist's customer, then that is a sale of goods. But if the substance of the contract, on the other hand, is that skill and labour have to be exercised for the production of the article and that it is only ancillary to that that there will pass from the artist to his client or customer some materials* in addition to the skill involved in the production of the portrait, that does not make any difference to the result, because the substance of the contract is the skill and experience of the artist in producing the picture."

He concluded there that the contract for the portrait was a contract for work and labour and materials.

88. Slesser LJ agreed, although he reached his decision on the particular facts of the case. Roche LJ having referred to ***Lee v Griffin*** said:-

"Equally, in my judgment, if the history and the reality of the transaction involved in the painting of a portrait of this kind is considered, it would be an abuse of language to say that the portrait is sold. In former days the phrase used would have been: "What painter are you going to employ to paint the portrait?". In these days the phrase is: "Who is commissioned to paint the portrait?". Both phrases are alike representative of a transaction which is a mandate or authority given to another for award to execute a certain thing which you desire - namely, the production of a portrait or representation of yourself or someone whom you wish to be so represented. That was the language, I think, employed in this case. The evidence as reported was that the defendant asked the plaintiff his fee for a portrait of Miss Finnegan, and then later the painter was commissioned to carry out the work.

In those circumstances, adopting the test put by Blackburn J. in ***Lee v. Griffin,*** *I have no doubt that the proper conclusion to be drawn is that this was a contract not for the sale of goods but for the employment of an artist to do work which the defendant desired that he should do."*

[3] His Honour Judge Bowsher QC in ***Corfield v Grant*** (1992) 59 BLR 102 at 112 accepted the reasons given by Stephenson LJ in Hutchinson v. Harris.

[4] This sitter later became the defendant's wife.

89. Secondly, Mr White relied upon ***Miles v. Wakefield MDC*** [1987] 1 AC 539. The issue in that case was whether a local authority who had appointed the plaintiff as a Superintendent Registrar of Births, Deaths and Marriages could deduct from his salary amounts representing periods when he had refused to work on Saturdays to conduct weddings, as part of industrial action. The House of Lords held that the council was entitled to make the deduction. Mr White relied upon the case since the Superintendent Registrar was to be regarded as a professional person, and because Lord Templeman concluded his speech by saying that the plaintiff was in no better position than a worker under a contract of employment in declining to work in accordance of the duties of his office (see page 565B). However Lord Templeman had prefaced that statement by saying that it was unnecessary to consider the law of damages and unnecessary for the employer to rely upon the defences and equitable set-off so little further assistance is to be gained from his speech. For the purposes of the appeal it had been accepted that there was no contract between the plaintiff and the Council. Lord Oliver of Aylmerton said in his speech (at page 567G):

"Nevertheless, the nature of his remuneration and the terms of his tenure of office are so closely analogous to those of a contract of employment that any claim by him to salary payable pursuant to the statutory provisions and the local scheme made thereunder ought, in my judgment, to be approached in the same way as a claim to salary or wages under such contract. The relationship between the Council and the plaintiff has all the incidents which one would expect from a contract of employment ... "

90. Accordingly, Lord Oliver also came to the conclusion that, applying that contractual analogy, the plaintiff could not successfully claim that he was in the circumstances of the case ready and willing to perform the work which he was properly required to do and therefore he was not entitled to be paid for the Saturday work (see pages 575H to 576A).

91. These cases and others (e.g. ***Sagar v. H. Ridehalgh & Sons*** [1931] 1 Ch 310) whilst of some assistance do not provide much support for Chevron's proposition that a contract for professional services is a contract for work and labour. Equally Mr Reese QC for Foster Wheeler could do little more than assert that the contract was one for professional services. The proposition of law that the defence of abatement is not available for contracts of professional services does not appear to have given rise to any decision as to whether a given contract was a contract for work and labour or was a contract for professional services. In the light of the authorities cited to me, in particular ***Robinson v. Graves,*** I am of the opinion that if the issue has to be approached as one of first principle then one must look at the relationship in question without any *a priori* assumption as to whether or not it was one for work and labour or for professional services; that one must look at the substance of the transaction rather than its form; and that one must, consistent with the foregoing, look at it in a contemporary context.

92. With these points in mind it is necessary to consider the factors which might be taken into account. First, and in favour of Foster Wheeler, Exhibit IV to the Contract expressly provides that the work is to be done by "an integrated Task Force Team of experienced and qualified engineers drawn from [Foster Wheeler's] own resources". This team is then described as a "multi-discipline team of engineers and designers". The organisation charts and lists of personnel show that many engineers are to be employed in varying grades, some of whom will undoubtedly have professional qualifications but others may be not so qualified. The personnel to be provided by Foster Wheeler also includes managers, draughtsmen and office and

93. Secondly, it is necessary to look at the scope of the work to be undertaken. Clause 2.1 of the contract require Foster Wheeler to "perform all designs, prepare all records, furnish or supplies and all items of a consumable nature that are required for design of the Facility in this Agreement and the documents listed immediately below...." I have already set out the relevant passages from clause 2.2 and other conditions, such as clause 3.1.2(c), and from Exhibit I which further describe the scope of the work. That Exhibit also sets out Technical Requirements which then describes further work that will need to be done: Project Support Services; "General Engineering which will include the examination of information and material supplied by Chevron; the coordination of weight control during designs; meeting with Vendors and visiting their sites, reviewing all vendor documentation, tender documents and submissions; preparing and providing a CADD model and data base; preparing documents required for submittal to the DOE pipe-line inspectorate and safety inspectorate certifying authority in DOT; providing for technical design review audits". Paragraph 3.3 required Foster Wheeler to provide Chevron with copy discs of structural analysis files. Section 4 made detailed provisions of the form in which documentation should be provided to Chevron and even covered the requirement to develop a control system for the purposes of the CTR Catalogue. Paragraph 2.4.1 of Exhibit II required Foster Wheeler to provide Chevron with office space.

94. Thirdly, Foster Wheeler's obligations were not, as I have already indicated, those ordinarily undertaken by professional people. In terms of the nature of the work to be done the contract was described as one for "Engineering/Design of Facilities to Accommodate Third Party Entrant Fields" and the split between engineering and design is reflected throughout the contractual documents - for example Exhibits II and IV drew a distinction between the design phases and the Follow-on Support Services and between Engineers and Designers. In consequence Foster Wheeler was contractually obliged not merely to exercise reasonable skill and care (due diligence and performance in accordance with generally accepted current good practice of the industry and trades involved) but was also under a contractual obligation to ensure that the Facility would be of a design which met the requirements of the agreement in that it would provide high operating reliability, minimum down type inoperable and would achieve an economical balance of first cost versus operating and maintenance cost

(see clause 2.2(a)). Clause 2.2(d) also required Foster Wheeler to "ensure that the Facility complied with the requirements of the agreement", and was able to operate satisfactorily in all conditions that might be encountered within the design parameters and was safe to operate and maintain etc". These obligations go considerably beyond the services ordinarily undertaken by a professional person and explain why the contract was one for engineering services as well

95. Finally, the contract was one for a variety of services, mainly but not exclusively of an engineering nature. Under it Foster Wheeler was required to achieve certain results, and as I have held, to secure the correction of errors, if necessary seeing that the offending work and equipment was put right so that the Facility met the requirements of the contract. Unlike a typical professional services contract Foster Wheeler was expected also to look at the equipment to be modified and, as I have described when considering Issue 3 above, if necessary to put right defects in the installations to be modified insofar as the defect or discrepancy might not have been detected by Foster Wheeler prior to the preparation of their design and also, if required by Chevron to put right not merely defects in the design but in the work itself resulting from any defects in Foster Wheeler's own designs. Accordingly Foster Wheeler was expected also to be effectively contractors.

96. In my judgment if a distinction has to be made between contracts for work and labour and those for professional services this contract falls into the former rather than the latter category. Undoubtedly skill and experience would be required in order to ensure that some of the contractual requirements were met (but no more than Mr Robinson was expected to apply skill and experience in the production of the portrait). However Foster Wheeler was nevertheless not engaged as consultants in the ordinary sense but as mechanical electrical and electronic engineering contractors over the border between consultancy and contracting. Foster Wheeler was required to provide a wide range of work and services resulting in the production of documents and computer generated discs which would set out the work product but it was also required to provide personnel to liaise with Chevron and with its fabrication and installation contractors and to be on hand both on-shore and off-shore to resolve queries and to see the project through to a satisfactory conclusion. Looking at the contract as a whole I am satisfied that it is not one for which would ordinarily attract the description of a contract for professional services to be performed by a party engaged in the oil industry work in the North Sea. It is in my view, for the purpose of legal categorisation, a contract for work and labour to which the defence of abatement is available.

97. Insofar therefore as Issue 1(b) has any practical impact, it is to be answered: No.

Mr Colin Reese QC and Mr Simon Lofthouse appeared for the plaintiff, instructed by Clifford Chance.
Mr Andrew White appeared for the defendant, instructed by Herbert Smith.