Alfred Mcalpine Construction Ltd v Panatown Ltd [1998] ABC.L.R. 02/05

On appeal from QBD (HHJ Fox-Andrews QC) sitting as a High Court Judge before Evans LJ; Hutchison LJ; Mantell LJ. 5th February 1998

LORD JUSTICE EVANS: This is the judgment of the Court:

Introduction

1. This appeal raises an issue of law under the Interim Award of an arbitrator, John H.M. Sims Esq., in a construction arbitration. The parties are the employer, Panatown Ltd., and the contractors, McAlpine, under a construction contract dated 3 November 1989. The contractors undertook to design and build an office building and multi-storey car park on a site in Cambridge on JTC standard terms. The contract price was in excess of £10 million.

2. The building was completed but Panatown alleges that it is seriously defective. So much so, that it may even have to be demolished and rebuilt. It remains empty and unused to this day, many years after Panatown gave notice terminating the contract of which they allege McAlpine was in breach.

3. Since then, the parties have become mired in what counsel have variously described as a quagmire and a morass of litigation and arbitration. The financial stakes undoubtedly are high. We are told that the sums in issue may be as much as £40 million. Even so, the present situation must be highly disturbing to anyone who shares current concerns at the astronomic cost of civil litigation (including arbitration), as the Courts do.

4. By contrast, the issue of law to which we have referred is crystal-clear. It cannot accurately be described as a short point, because we have heard four days of argument and counsel cannot be criticised, given the present state of the authorities and our current procedures, for presenting the appeal in this way. But the issue is capable of concise definition, and before quoting the question raised by McAlpine in their Notice of Motion, by which the appeal proceedings were commenced, we shall define it in this way.

5. Panatown, although the employers under the construction contract, were not and have never been the owners of the construction site. The *"building owners"*, so described in contemporary documents, were their associated company Unex Investment Properties Ltd. ("UIPL"). UIPL were both the owners of the site and, broadly, the developers who sought to have the building constructed on it. But they did not enter into the construction contract themselves. Rather, Panatown did so. Both UIPL and Panatown are members of the same group, the parent company being Unex Corporation Ltd. These arrangements were made for a specific purpose. This was to avoid the construction contract becoming liable to VAT which was not imposed on contracts for new buildings until September 1989. Before that date, UIPL paid £7.5 million, a substantial part of the estimated building cost, to Panatown, and in the event no VAT liability was incurred on the construction contract between Panatown and McAlpine, even though it was entered into after the imposition of VAT.

6. Panatown commenced arbitration proceeding against Mcalpine in 1992/3, claiming damages for what it alleges were defective works. In early 1994 McAlpine raised the issue of law with which we are concerned. They say, quite simply, that Panatown is not entitled to recover damages for the alleged breaches of contract, because Panatown is not and never has been the owner of the site. Therefore, the argument runs, the loss which Panatown claims by reason of the allegedly defective condition of the building has been suffered not by Panatown but by UIPL, the developer and owner of the site. So Panatown cannot recover more than nominal damages, even if the breaches of contract are proved. Nor can UIPL recover damages for breach of this contract, to which they were not parties, nor are they parties to the arbitration.

   (There was another contract between McAlpine and UIPL, to which further reference will be made below, but it does not contain an arbitration clause and there could not be a single arbitration, even if it did.)

7. The arbitrator, who by agreement between the parties heard the preliminary issue with Brian Knight Q.C. as legal assessor, held that Panatown is not debarred from recovering substantial damages, if the alleged breaches are proved, and McAlpine's suggested legal defence therefore failed. The official referee, Judge Anthony Thornton Q.C., reached the opposite conclusion on this central issue of law, although he remitted the Interim Award to the arbitrator so that some further aspects of it might be considered.

8. Panatown now appeals. The question of law was defined in McAlpine's Notice of Motion as follows:- *"Do Panatown's claims for (a) liquidated damages for delay (b) unliquidated damages for delay and failure to complete and (c) damages for defective and/or incomplete work (or any and if so which of them) fail (insofar as they relate to greater than nominal damages) because Panatown is not the owner of the property?"*

9. The appeal was by consent of both parties, and so the terms of the question were not defined by the Court at that preliminary stage. There has since been a plethora of re-formulations and re-re-formulations, by the parties and by the judge, but none of these, we are told, has been agreed by both parties in substitution for the original definition in the Notice of Motion. Whether the Court does have power to re-formulate the question, without the consent of the parties, is a somewhat arid procedural issue to which we shall return if it becomes necessary for us to do so.

10. We propose to escape at least temporarily from the quagmire of other proceedings and the procedural complications which have beset this appeal from the Interim Award by concentrating initially on the question as formulated above. We shall also concentrate on the damages claim for allegedly defective work, as counsel have done in their submissions to us. So the question becomes: are Panatown debarred from recovering substantial as opposed to nominal damages, by reason of the fact that they were not, and are not, owners of the land?

11. The starting point, agreed by both parties and never in doubt, is that the innocent contracting party is entitled to recover damages from the party in breach amounting to compensation for the loss which he has suffered in consequence of the breach.

The issue

12. The appeal is presented to us in a way which we hope that we can summarise as follows, without doing injustice to the submissions of counsel:-

(1) There is a general rule of English law, that a person cannot recover substantial damages for breach of contract where he himself has suffered no loss by reason of the alleged breach. "Substantial" is used in distinction from "nominal" damages, because the breach of contract is actionable without proof of damage. The rule, essentially, is that the plaintiff cannot recover compensation for the consequences of the breach when the actual loss has been suffered, in the particular circumstances, not by him but by a third person who was not a party to the contract.

(2) An exception to this rule was established by the judgment of Lord Cottenham L.C. in ***Dunlop v. Lambert*** (1839) 6 Cl. & F.600. The exception is that the consignor of goods can recover damages for loss of or damage to the goods in the course of their carriage even if the goods have become the property of a consignee before the loss or damage occurs.

(3) This exception was upheld by the House of Lords in ***The Albazero*** [1977] A.C. 774 where it was also held, however, that the exception does not apply when the parties to the original contract (consignor and carrier) contemplate that a separate contract will come into existence between the carrier and consignee, regulating the liabilities between them. That is invariably the case where the parties to a charterparty know that a bill of lading will be issued and endorsed to a consignee. Such was the situation in ***The Albazero*** and so the consignor's claim failed in the House of Lords (it was upheld reluctantly by the Court of Appeal in the light of the **Dunlop v. Lambert** decision: per Roskill L.J. at 822).

(4) The exception or special rule in ***Dunlop v. Lambert*** was extended to building contracts, enabling the employer to recover substantial damages from the contractor, by the House of Lords in ***St Martins Property Corporation v. Sir Robert McAlpine Ltd*** [1994] 1 A.C. 85 (sub. nom. ***Linden Gardens Trust Ltd)*** where the employer owned a proprietary interest in the land at the time of the contract, although he parted with it before any breach of contract occurred, and by the Court of Appeal in **Darlington B.C. v. Wiltshier Northern Ltd** [1995] 1 W.L.R. 68 where he never had such an interest.

(5) In the ***St Martins*** case, Lord Griffiths decided in the employer's favour on a broader ground, namely, that the right to recover more than nominal damages for breach of a contract to supply work, labour and materials, nominal damages apart, was not dependent upon the plaintiff having a proprietary interest in the subject-matter of the contract at the date of the breach (see p.96F). Other members of the House of Lords expressed sympathy with this view, but none adopted it as a ground for decision (see pages 95E, 96A, and 98G and 112E).

(6) Two issues arise therefore in the present case:-

(i) is the rule, or exception, in ***Dunlop v. Lambert*** excluded, because there was a contract between the contractors (**McAlpine)** and UIPL (described as the "building owner", and in fact the owner of the building land) which displaces the employer's right to recover substantial damages, as occurred in ***The Albazero*** ?

(ii) are Panatown entitled to recover substantial damages on the "broader" ground defined by Lord Griffiths in ***St Martins ?***

13. As emerged in the course of argument, and as will be apparent from this summary, there is some scope for confusion, or at least for semantic uncertainty, in the formulation of the issues. What is the rule, and what is the exception? What is the relationship between the ground on which ***St Martins*** was decided by the majority and the "broader ground" upon which Lord Griffiths relied (the term was used by Lord Keith of Kinkel at page 95E)? If St ***Martins*** applied a ***Dunlop v. Lambert*** "exception", does the broader ground represent a separate rule, and if it does, how is that to be reconciled with the so-called general rule?

14. It seems to us that these difficulties are resolved if the issues are slightly re-defined in the light of the judgments to which we have referred.

(1) Dunlop v. Lambert

The only relevant paragraph (see per Lord Diplock in ***The Albazero***_at 843G) from the lengthy judgment reads as follows:- *"These authorities, therefore, establish in my mind the propositions which are necessary to be adopted, in order to overrule this direction of the Lord President. I am of opinion, that although, generally speaking, where there is a delivery to a carrier to deliver to a consignee, he is the proper person to bring the action against the carrier should the goods be lost; yet that if the consignor made a special contract with the carrier, and the carrier agreed to take the goods from him and to deliver them to any particular person at any particular place, the special contract supersedes the necessity of showing the ownership in the goods; and that, by the authority of the cases of Davis v. James 5 Burr 2680 and Joseph v. Knox, 3 Camp. 320, the consignor, the person making the contract with the carrier, may maintain the action, though the goods may be the goods of the consignee."* (pages 843-44)

The decision therefore was that a "*special contract*" between consignor and carrier may "*supersede the necessity of showing the ownership in the goods"*. As Lord Diplock pointed out in **The Albazero** (page 843B), no clear distinction was drawn in earlier authorities between the right of the consignor to sue under a "special

contract" with the carrier and the measure of damages sc. substantial damages which he was entitled to recover. ***Dunlop v. Lambert*** therefore upheld a contractual right to recover damages which had the effect of creating an exception to any general rule that a plaintiff could not recover damages for a loss which he had not himself suffered, but this was the result of rather than the reason for the decision. And the result followed from what the parties to the contract had agreed, not from what was said to be an exception to the general law.

(2) Lord Diplock re-affirmed the contractual basis for the ***Dunlop v. Lambert*** decision after his thorough review of the authorities in ***The Albazero***. He referred to Counsel's submission that the rule (sic) which it was understood to have laid down was an *"anomalous exception"* to the general law regarding the recovery of damages (page 845G), but he appears not to have accepted this formulation. He stated his conclusion as follows:-

"The only way in which I find it possible to rationalise the rule in ***Dunlop v. Lambert*** *so that it may fit into the pattern of the English law is to treat is as an application of the principle, accepted also in relation to policies of insurance upon goods, that in a commercial contract concerning goods where it is in the contemplation of the parties that the proprietary interests in the goods may be transferred from one owner to another after the contract has been entered into and before the breach which causes loss or damage to the goods, an original party to the contract, if such be the intention of them both, is to be treated in law as having entered into the contract for the benefit of all persons who have or may acquire an interest in the goods before they are lost or damaged, and is entitled to recover by way of damages for breach of contract the actual loss sustained by those for whose benefit the contract is entered into."*(page 847)

As well as the express reference to "*the contemplation of the parties*", meaning the consignor and carrier as parties to the relevant contract of carriage, the parallel drawn with insurance cases is, in our judgment, significant. The leading case which Lord Diplock cited at p.846F was ***Waters v. Monarch Fire and Life Assurance*** (1856) 5 El. & Bl. 870. This was authority for the proposition that the insured can recover the full value of loss and damage to goods "on behalf of anyone who may be entitled to an interest in the goods at the time when the loss or damage occurs, provided that it appears from the terms of the policy that he intended to cover their interests" (page 846F cf. The Marine Insurance Act 1906 section 26(3)). These references to the terms of the policy and the insured person's intention underline the contractual nature of a rule which Lord Diplock traced back to its origins in the law merchant (see page 846B).

(3) Likewise, the qualification which meant that the rule did not apply in ***The Albazero*** was also stated in terms of the intention of the parties to the relevant i.e. the original contract:- *"The rationale of the rule is in my view also incapable of justifying its extension to contracts for carriage of goods which contemplate that the carrier will also enter into separate contracts of carriage with whoever may become the owner of goods carried pursuant to the original contract."*(page 847)

This led to the conclusion that:- *"The complications, anomalies and injustices that might arise from the co-existence in different parties of rights of suit to recover, under separate contracts of carriage which impose different obligations upon the parties to them, a loss which a party to one of those contracts alone has sustained, supply compelling reasons why the rule in* ***Dunlop v. Lambert*** *, 6 Cl. & F. 600 should not be extended to cases where there are two contracts with the carrier covering the same carriage and under one of them there is privity of contract between the person who actually sustains the loss and the carrier by whose breach of that contract it was caused."* (page 848).

Lord Diplock had already referred to the carrier's liability to the consignee, when the property in the goods has passed to him, in an action in tort (see page 844G). It is not the existence of legal liability, therefore, or of the consignee's right to recover damages from the carrier, which precludes the ***Dunlop v. Lambert*** approach in cases such as ***The Albazero ,*** but the fact that the parties to the original contract contemplate that the carrier will enter into a separate contract of carriage of the kind which Lord Diplock described. The rule (sic) applies when the parties to the original contract contemplate that the consignor will be entitled to recover substantial damages under that contract, even when he is no longer the owner of the goods, if he chooses to do so. He has contracted "*on behalf of*" the person who has become the owner. It is also clearly established that he holds any damages which he recovers in respect of an interest which he does not own "*on account of*" the owner of the interest; in common law terms, he was liable under an action for money had and received at the suit of that other person (page 845B).

(4) ***St Martins*** was a case where it was known to both parties to a building contract that the development "was going to be occupied, and possibly purchased, by third parties and not by the employer himself" (per Lord Browne-Wilkinson at 114G). The rationale of ***Dunlop v. Lambert*** was applied, although this was described as an exception to the general rule that the plaintiff can only recover damages for his own loss (ibid). Again, the contractual basis was emphasised:-

"In such a case, it seems to me proper, as in the case of the carriage of goods by land, to treat the parties as having entered into the contract on the footing that Corporation would be entitled to enforce contractual rights for the benefit of those who suffered from defective performance but who, under the terms of the contract, could not acquire any right to hold McAlpine liable for breach. It is truly a case in which the rule provides "a remedy where no other would be available to a person sustaining loss which under a rational legal system ought to be compensated by the person who has caused it." (page 115).

(5) In ***St Martins*** the employer held a proprietary interest in the land at the date of the building contract. In ***Darlington B.C. v. Wiltshier*** he did not. He had only a financial interest in the project and he had undertaken to assign all his rights and causes of action against the contractor to the plaintiff Council, which owned the site. All three members of the Court were prepared to apply directly what Dillon L.J. described as "*the rule in* ***Dunlop v. Lambert*** *as recognised in a building contract context in Lord Browne-Wilkinson's speech in the McAlpine [* ***St Martins*** *] case*" (page 75B. cf. Steyn L.J. at 80C and Waite L.J. at 81B). Dillon L.J. reached the same result by holding that the employers were constructive trustees on behalf of the Council, applying ***Lloyd's v. Harper*** (1880) 16 Ch. D. 290 also (page 75E), and Waite L.J. agreed (page 81C). In addition, Steyn L.J. agreed with and was prepared to apply "*the wider principle*" stated by Lord Griffiths in **St Martins** . The point had been argued in some depth and was based on "classic contractual theory" (page 80E-F). Dillon L.J. referred to Lord Griffiths' speech but it was unnecessary for him to consider it further, and by implication Waite L.J. agreed (pages 75F and 81B-C).

(6) ***St Martins*** and ***Darlington*** therefore were both cases in which the rule (or exception) in ***Dunlop v. Lambert*** was applied in the context of a building contract. The employer was entitled to recover substantial damages for the contractor's failure to carry out the work in accordance with his obligations under the contract, notwithstanding that he was not the owner of the land. In ***Darlington*** the plaintiff was the assignee of the employer's rights and he could only recover the same measure of damages as the employer, his assignor; hence the need to establish whether the employer was entitled to recover substantial damages, or not (see page 72H). In both cases, the claim was for damages for bad workmanship (***Darlington*** at page 72B) or for failure to construct the building of sound materials and with all reasonable skill and care (***St Martins*** at 96D) and there was no doubt what the appropriate measure of damages was, if the employer was entitled to recover substantial damages. The contractor is liable for the cost of remedying the defective work (***East Ham Corporation v. Bernard "Sunley & Sons Ltd [***1966] A.C. 406) although in certain circumstances the damages may be limited to the diminution in value resulting from the breach (now established by ***Ruxley Electronics and Construction Ltd. v. Forsyth [***1996] A.C. 344).

(7) Finally, both cases were distinguished from ***The Albazero*** where *Dunlop v. Lambert* was not applied because the parties to the original contract of carriage, the charterparty, contemplated that bill of lading contracts would be issued which would be endorsed to the consignee, if property in the goods was transferred to him. In ***St Martins*** , no such contractual arrangements were contemplated, though Mr Fernyhough Q.C., counsel for the contractors submitted that there could be other cases where the contractors entered into direct warranties with the ultimate purchasers of the individual parts of a development (page 115D). Lord Browne-Wilkinson said this:- *"As to the warranties given by contractors to subsequent purchasers, they will not, in my judgment, give rise to difficulty. If, pursuant to the terms of the original building contract, the contractors have undertaken liability to the ultimate purchasers to remedy defects appearing after they acquired the property, it is manifest the case will not fall within the rationale of* ***Dunlop v. Lambert*** *6 Cl. & F.600. If the ultimate purchaser is given a direct cause of action against the contractor (as is the consignee or endorsee under a bill of lading) the case falls outside the rationale of the rule. The original building owner will not be entitled to recover damages for loss suffered by others who can themselves sue for such loss. I would therefore hold that Corporation is entitled to substantial damages for any breach by McAlpine of the building contract."* (page 115).

In ***Darlington*** there was a contract between the contractor and the Council, the owner of the site. Dillon L.J. explained the position thus:- "As supplemental to each of the building contracts and of the same date a tripartite deed was entered into by Morgan Grenfell, Wiltshier and the council which gave the council direct contractual rights against Wiltshier for any liquidated damages for failure to complete the construction of either phase on time under the building contracts. In the events which have happened there has been no occasion for the council to seek to claim liquidated damages. But the fact that such provision was made for the liquidated damages in the tripartite deed is relied on by Mr Blackburn for Wiltshier, as an indication that the council has no right to any other damages as against Wiltshier as no comparable provision was made for other damages. As I see it, that is not a point of great weight. For the liquidated damages to be recoverable, it would be necessary to show that they were a fair pre-estimate of loss which would be occasioned by delay in completion of the Dolphin Centre. But the liquidated damages could only be a fair pre-estimate of loss occasioned by delay in completion if they were payable to the council to compensate the council's loss. Delay in completion plainly would not cause Morgan Grenfell any loss at all." (page 71).

This suggests that any liquidated damages which the Council was entitled to recover under the Deed were those provided for in the building contract between the employer (Morgan Grenfell) and the contractor. Such a provision would be unenforceable as a penalty if relied upon by the contractor in his own right. Dillon L.J. refers to the possibility of the Council recovering liquidated damages (under the deed) if they were a genuine pre-estimate of its own loss. Clearly, he did not consider that such a right would have prevented the employer from recovering substantial damages for breach of the building contract, as regards bad workmanship, in accordance with ***Dunlop v. Lambert*** .

Conclusion

15. There is clear House of Lords authority that in at least two kinds of cases a contracting party can recover substantial damages for breach of contract notwithstanding that the financial loss which is the measure of damages has not been borne by him. The consignor of goods is entitled to recover damages for loss of or damage to the goods, for which the carrier is liable under the contract of carriage, even when the goods have

become the property of the consignee. That is the decision in ***Dunlop v. Lambert*** which was confirmed in ***The Albazero*** subject to the qualification that the parties must have intended that the consignor should have that right. (**The Albazero** itself was within the qualification because no such assumption could be made.) The second case is that of the employer under a building contract where the employer claims damages for defective work (St Martins). The same qualification applies (per Lord Browne-Wilkinson at 115E). There is similar authority, in our judgment, that the same rule applies in relation to claims under insurance cover against loss of or damage to goods (that is, the insurance cases approved by Lord Diplock in ***The Albazero***) and that the consigner of goods can recover damages for loss or damage for which the carrier is liable under the contract of carriage as though he were the owner of the goods notwithstanding that he had only a limited interest in the goods e.g. as bailee when he consigned them for carriage. This was the common law rule as regards claims against a wrongdoer in tort, though largely for historical reasons (***The Winkfield*** [1902] p.42; see now Torts (Interference with Goods) Act, 1977, section 7), which again was referred to with approval by Lord Diplock in this context in ***The Albazero*** (page 846C).

16. If this analysis is correct, then in our judgment ***Dunlop v. Lambert*** establishes that the right to recover "substantial *damages"*, meaning the appropriate measure of damages, arises because the parties to the contract intended or contemplated that it should arise, their intention being ascertained from the terms of the contract and the circumstances in which it was made, in the usual way. This is, in our view, the "*classic contractual theory*" to which Steyn L.J. referred in ***Darlington.*** When this situation arises, the plaintiff recovers damages in respect of financial loss which in fact has been borne by another person, and he is liable to account to that other person accordingly. The result therefore can be described as an "*exception*" to the general rule that a plaintiff cannot recover damages in respect of another person's loss, but equally it is simply equivalent to saying that the general rule can be modified by agreement, express or implied, between the parties concerned.

17. The *"broader ground*" or "*wider principle*" which Lord Griffiths recognised in ***St Martins*** was quite narrowly stated by him:- *"I cannot accept that in a contract of this nature, namely for work, labour and the supply of materials, the recovery of more than nominal damages for breach of contract is dependent upon the plaintiff having a proprietary interest in the subject of the contract at the date of the breach."* (page 96G).

18. Lord Griffiths held that in such cases the contracting party can recover damages for the "*loss of bargain*" caused by the defendant's breach. The fact that he is not the owner of the property concerned does not disqualify him from recovering *"the normal measure*" of that loss (page 96D). Lord Browne-Wilkinson considered the implications of this approach in two other kinds of case: sale of goods (pages 111F-112B) and contracts for the supply of goods or services to a third party (page 112C). As regards the former, we were referred to the recent judgment of this Court in ***Bence Graphics International Ltd v. Fasson U.K. Ltd*** [1997] 1 All E.R. 979, and as regards the latter **Woodar Investment Developments Ltd. v. Wimpey Construction U.K. Ltd** [1807] 1 W.L.R. 277 where the decision in ***Jackson v. Horizon Holidays Ltd*** [1975] 1 W.L.R. 1468 (C.A.) was commented upon. In ***St Martins*** Lord Keith of Kinkel referred generally to "*other forms of commercial contract*" (page 95F).

19. The House of Lords did not hear full argument on this "broader" issue, and Lord Browne-Wilkinson said this about it:- *"I am reluctant to express a concluded view on this point since it may have profound effects on commercial contracts which effects were not fully explored in argument. In my view the point merits exposure to academic consideration before it is decided by this House."* (page 112F).

20. Counsel in the present case with commendable diligence have placed before us a total of eleven articles and case-notes which comment upon or are relevant to the ***St Martins*** decision, together with extracts from ten leading text-books. We also have the Law Commission's Report "Privity of Contract: Contracts for the Benefit of Third Parties" (1996 No. 242) where the recovery of damages for a third party's loss (distinct, in our view, from the question of whether a third party is or should be entitled to sue under a contract to which he is not a party) was also discussed. So far as counsel and we are aware, the books do not contain any in-depth analysis of the issue, and no academic writer, so far, has responded to Lord Browne-Wilkinson's invitation. We do not feel, however, that we are disadvantaged as a result, because we have had the benefit of submissions from Mr Friedman Q.C. for the employers and Mr Jackson Q.C. for the contractors and an extensive citation of authority which can only have been based on learning and wide-ranging research of the highest quality, of which even the most distinguished academic writers would be proud. We are greatly indebted to them.

21. In these circumstances, we would hold that the rationale of ***Dunlop v. Lambert*** and ***St Martins*** is contract-based, for the reasons we have sought to express above, and that ***St Martins*** is direct authority that this approach should be adopted when the claim is for damages for defective work by the employer against the contractor under a building contract of this kind. The "*broader"* issue is not, we would suggest, a possible alternative route to the same conclusion. Rather, it is the underlying principle on which the ***Dunlop v. Lambert*** and ***St Martins*** decisions are based. This leaves open the question whether a similar contract-based approach can and should be adopted in other kinds of case. It is unnecessary to consider this further in a building contract case, because the House of Lords has held that it can. We would add, however, in respectful agreement with Lord Browne-Wilkinson, that it does provide a clear and satisfactory explanation of the reason why a contracting party can sometimes, but not always, recover damages in respect of loss which in fact has been suffered by a third party, on whose behalf he can be said to have contracted, and why the measure of damages in sale of goods cases depends ultimately on what was intended, or contemplated, by the parties (***Bence Graphics*** above).

22. For these reasons, we would hold that the question whether the appellants are entitled to recover substantial damages in the present case depends upon what inference should be drawn as to what they intended and contemplated when the contract was made. ***St Martins*** is direct authority that they are not debarred from doing so by the fact that they are not, and never were, the building owners. The remaining issue is whether the contractual rights given to the building owners against the contractors direct were such as to preclude the ***Dunlop v. Lambert*** approach, as they did in a different context in ***The Albazero .***

The building contract

23. The building contract is in JCT Standard Form with Contractor's Design (1981 ed. amended in 1986). It incorporates the elaborate and detailed terms which are usual in contracts of this kind. The contractor undertakes to carry out and complete the contracts upon and subject to the Conditions (clause 2.1) and he gives a design warranty in terms that he:- *"Shall have in respect of any defect or insufficiency in such design the like liability to the Employer, whether under Statute or otherwise, as would an architect or .... other appropriate professional designer holding himself out as competent to take on work for such design who, acting independently under a separate contract with the Employer, had supplied such design for or in connection with works to be carried out and completed by a building contractor not being the supplier of the design"* (clause 2.5.D.).

24. The contract procedures, in summary, enable the contractor to recover stage payments and the employer may withhold payment on account of defective or non-contractual work. A right to terminate the contract is given to the employer by clause 27, and Panatown claims to have exercised that right in the present case. The contract price was £10,436,696 and there is provision for arbitration in common form (Art. 5 and clause 39). Article 4a reads as follows:- *"The works shall be designed and built to a standard generally suitable for use and occupation as high class offices by companies or partnerships requiring the whole of the buildings ... ",*

and clause 18.1, dealing with assignment, was amended in manuscript to read (manuscript words underlined):- "*Neither the Employer nor the Contractor shall, without the written consent of the others, assign this Contract, which shall not be unreasonably withheld .*"

The Duty of Care Deed

25. On the same day as the building contract, 2 November 1989, the contractors (Alfred McAlpine Construction Ltd.) entered into a Deed with UIPL, described as "the Building Owner", in the following terms:-

"(A) By an agreement ("the Building Contract") made between the Contractor and Panatown Limited acting on behalf of the Building Owner the Contractor agreed to construct the Current Development.

(B) The Contractor has agreed to enter into this Agreement with the Building Owner.

1. WARRANTIES

The Contractor undertakes with the Building Owner that in respect of all matters which lie within the scope of his responsibilities under the Building Contract

(a) he has exercised and will continue to exercise all reasonable skill care and attention;

(b) he shall owe a duty of care to the Building Owner in respect of such matters;

2. ASSIGNMENT

The contractor agrees that the building owner may assign or charge the benefit of this agreement to its successors in title to the current development or any part of it or to any other party with the consent of the contractor, which shall not be unreasonably withheld.

5. LIMIT OF LIABILITY

Except in relation to the Contractor's obligations under Clauses 1.01(d), 1.02 and 2 hereof, the Contractor shall have a no greater liability to the Building Owner under this Agreement than it would have under the Building Contract, if the Building Owner was named therein as the Employer."

Issues

1. Did the parties to the building contract intend (or contemplate) that the employer, Panatown, should be entitled to recover substantial damages for defective work, notwithstanding that it had no proprietary interest in the land?

26. In our judgment, the ***St Martins*** and ***Darlington*** decisions are direct authority that the answer to this question must be "yes", subject to the further question whether the Duty of Care Deed entered into on the same date between the contractor and the building owner brings the case within same category as ***The Albazero*** (issue (2) below). With that proviso, the correct interpretation of this contract, in our view, is clear. The employer is not required to pay for defective work. If sued for the price, he could deduct the amount of any damages for which the contractor was liable for defective work from the amount he was otherwise liable to pay (the principle of abatement: ***Gilbert-Ash (Northern) Ltd v. Modern Engineering (Bristol) Ltd*** [1974] A.C. 689). Put shortly, both parties contemplated that accounts would be settled between them, and if the employer was not entitled to recover damages for defective work, or for failure to complete the works, then an anomaly would arise and the parties' expectations would be defeated. We should add that there is no reported case where the contractor has defeated a damages claim by the employer on this ground. None was cited in **St Martins** or **Darlington** and none has been cited to us. ***West v. Houghton*** (1879) 4 C.P.D. 197 was relied upon by Mr Jackson, but the circumstances were entirely different and in our judgment it does not provide a useful guide to ascertaining what was intended or contemplated by the parties to a modern construction contract (an estate owner recovered no more than nominal damages from a bailiff who had contracted to clear the land of rabbits, because the crops that were damaged were the property of his tenant).

(2) Do the existence and terms of the Duty of Care Deed lead to a different conclusion?

27. Although the DCD is only a contract between the contractors and the building owner i.e. the owner of the site, it was entered into on the same day as the building contract and clearly it can be inferred that the two contracts were intended to take effect and to be read in conjunction with each other.

28. Equally clearly, the DCD created and was intended to create a right of action in contract for the building owner against the contractor, if the contractor was in breach of its terms. This would enable the building owner to recover damages which he might suffer in consequence of the breach. The contractor's obligations under this contract were largely co-extensive with those under the building contract, but they were expressed differently. The most striking difference is that the building contract, apart from the design warranty in clause 2.5 (assuming that this is intended to impose a standard of "*reasonable skill and care*", rather than an absolute standard, although we are not sure that that is correct), tends to require the contractor to carry out works in accordance with the contract specification, not merely to exercise reasonable skill and care in attempting to do so. In practice, the difference may be less than might be supposed, but it is significant in legal terms. The duty of care is defined by reference to the scope of the contractor's responsibilities under the building contract (clause 1) but clause 5 imposes a limit on the contractor's liability by reference, in one way or another, to its liability under the building contract (again, the meaning is not entirely clear, in our view).

29. Mr Friedman submitted that the duty of care deed was intended to apply only to the contractor's design obligations, because the limit of the insurance cover required by clause 1(d) (not quoted above) is £3 million. That figure may be appropriate for breach of the design warranty, but it is substantially less than the contract price or the possible cost of remedying major construction defects. However, we do not consider that this is a sufficient reason for limiting the scope of clauses 1 and 5, which embrace the whole of the contractor's responsibilities under the building contract.

30. The DCD is undoubtedly a separate contract from the building contract and the building owner is regarded as a separate person, not itself being the employer under the building contract. True, the Deed recites that Panatown made the building contract "*acting on behalf of*" the building owner, and clause 5 has regard to what the contractor's liability would be if the building owner "*was named therein as the employer*", rather than, for example, *"was a party thereto*" or "*the employer thereunder*". However, it is not suggested that Panatown was acting as agent for UIPL or that UIPL is a party to the building contract (apart from the faint suggestion of a constructive trust, to which we shall refer below) and in our judgment the DCD properly regarded is a separate contract between the contractor and the building owner as a third party to the building contract.

31. This is confirmed by the terms of the Deed, because the duty of care which the contractor undertakes under clause 1 corresponds with the liability which the general law would impose upon him, sometimes with regard to foreseeable financial or economic loss, as regards a third party known to be interested in the construction project.

32. We were told by Mr Friedman that contracts of this sort are frequently entered into and that their commercial purpose is clear and well-known. The building owner even where he is the employer under the building contract will forseeably intend to sell or let the property to purchasers or tenants who will have no contractual claims against the contractor except by the cumbersome and complicated method of assigning the employer's rights under the building contract to them. Hence the warranties referred to by Lord Browne-Wilkinson in ***St Martins*** (page 115) and the form of duty of care deed entered into in the present case. Here, the form was used to create contractual relations between the contractor and the building owner where he was not the employer. Clause 3 of the DCD (not quoted above) permits assignment to the building owner's *"successors in title to the Current development or any part of it"* with the consent of the contractor "*which shall not be unreasonably withheld*". The commercial purpose, therefore, was the same.

33. Mr Jackson submits that the parties clearly intended that the building owner should have separate contractual rights, independently of the building contract, and that the ratio of ***The Albazero*** decision therefore applies. The fact that the contract terms are not identical makes it an ***a fortiori*** case (per Lord Diplock at p.848C).

34. Mr Friedman too relied upon the fact that the contractor's basic obligation under the DCD is wholly distinct from its liabilities under the building contract. A general duty of care, with or without whatever limitation is imposed by clause 5, is a different concept from the contractual scheme under the building contract. His skeleton argument includes this sentence:- *"It is an extraordinary proposition that, because there is a duty of care deed which gives a limited warranty to the building owner, the employer should be unable to enforce any of his rights under the building contract by claiming damages".*

35. A further consideration is that McAlpine's parent company guaranteed its performance of the building contract, but there is no guarantee of its liabilities under the DCD.

36. If there is a rule of law, to the effect that the employer cannot recover substantial damages "*on behalf of*" the building owner when there is a separate contract between the building owner and the contractor under which substantial damages, though not necessarily the same measure of damages, could be claimed by the building owner direct from the contractor, then it would seem to follow from ***The Albazero*** that the employer is disentitled from doing so in the present case. It might be possible as a matter of law to distinguish a building contract from a contract for carriage by sea on the ground that the bill of lading which the parties contemplate will be issued has a special status and is different from a warranty or duty of care deed between the contractor and some party other than the employer. However, in our judgment, that is not the correct approach.

37. It seems to us, consistently with what we have called the contract-based approach to the question whether the employer is entitled to recover substantial damages, as in ***St Martins ,*** that the issue is one of construction, the contract in question being that under which substantial damages are claimed. Given that the parties contemplated that the separate contract would be entered into (in ***Darlington*** there was a tripartite deed, though limited it appears to liquidated damages for delay), they may, or may not, intend and contemplate that the right given to the building owner (third party) to recover damages himself will displace the right which otherwise the employer would have, to recover substantial damages on his behalf. Whether they did so or not depends upon the construction of their contract and the circumstances in which it was made. If there was an independent commercial reason why the separate contract was entered into, and its scope is markedly dissimilar to that of the original contract, then the likelihood that it was intended to displace or vary the effect of what the parties agreed between themselves is correspondingly less.

38. In our judgment, this approach leads to the clear conclusion that the DCD was not intended to preclude the employer's right to receiver substantial damages under the building contract in the present case. The parties to that contract cannot have intended or even contemplated that the elaborate provisions of the standard form of contract, which they amended in many respects so as to have a tailor-made version for the particular project, could be replaced by a claim for damages, on a different basis, before a Court rather than in arbitration under the building contract (there is no arbitration clause in the DCD). We would hold that, on the true construction of their contract, the parties did not intend or contemplate that the DCD should deprive the employers of the right to claim substantial damages for the contractor's breach.

39. The conclusion could be justified on narrow semantic grounds by reference to the wording of the recital to the DCD: Panatown entered into the building contract *"on behalf of"* UIPL. That is consistent with phrases used in ***The Albazero*** and ***St Martins .*** That ground, in our view, would not be enough if it stood alone, but it is re-assuring that the legal result is what the parties considered it to be.

40. Mr Jackson placed much emphasis on the risks of double recovery, and it is of course inevitable that the building owner does have the right to make a separate claim for damages in Court proceedings under the DCD. This dichotomy has produced many of the procedural complications which exist (and which have, apparently, been much exploited by both parties) in the present case. These risks and difficulties arise, in our view, from the fact that there are two contracts rather than from the fact that the employer is entitled to recover substantial damages in the circumstances of this case. He is entitled to do so, if our approach is correct, because both parties intended that he should. The risk of double recovery has been recognised since the nineteenth-century: see e.g. ***The Winkfield*** [1902] P. at page 60:- *"His obligation to account to the bailor is really not ad rem in the discussion. It only comes in after he has carried his legal position to its logical consequence against a wrongdoer, and serves to soothe a mind disconcerted by the notion that a person who is not himself the complete owner should be entitled to receive back the full value of the chattel converted or destroyed. There is no inconsistency between the two positions; the one is the complement of the other".*"

(See also ***The Albazero*** at page 845B). The common law solution has been that the claimant who recovers damages in respect of a proprietary interest that he does not own is liable to a claim by the owner for money had and received. It seems to us that there will be no risk of double recovery if damages are recovered by the employer "*on behalf of*" the building owner, and that such damages would have to be taken into account if the building owner made a separate claim. The legal mechanisms would not be difficult to devise. The perhaps remote risk of inconsistent decisions in arbitration and in the Courts arises from the fact of separate contracts, only one of which contains an arbitration clause, and it can only be guarded against by procedural means.

Constructive Trust

41. Mr Friedman made a passing reference to the possibility of the employer maintaining his claim as constructive trustee for the building owner as beneficiary, but he did not develop the submission before us. It may be that ´constructive trust' is a correct description of the same rules of law in an equitable guise, but it is unnecessary to say more.

Conclusion

42. We would hold that the issue of law should be answered as indicated above. This suggests that question (c) in the Notice of Motion should be answered "No". The appropriate form of question and answer can be considered at a further hearing when outstanding issues as to remission etc. will be dealt with. Any further submissions on questions (a) and (b) - damages and liquidated damages for delay - can be heard at the same time.

ORDER: No order.

MR RUPERT JACKSON QC and MR PAUL SUTHERLAND (instructed by Messrs Ashurst Morris Crisp, London EC2A 2HA) appeared on behalf of McAlpine construction Limited.
MR DAVID FRIEDMAN QC and MR JEREMY NICHOLSON (instructed by Messrs Masons, Manchester M5 3EJ) appeared on behalf Panatown Limited.