CA on appeal from QBD, Official Referee's Business (His Honour Judge Wilcox) before Lady Justice Butler-Sloss, Hobhouse LJ, Buxton LJ. 15th October 1997.

LADY JUSTICE BUTLER-SLOSS: I will ask Buxton LJ to give the first judgment.

LORD JUSTICE BUXTON:

1. The appellants (Mellowes) were subcontractors to the respondents (Bell), who in turn were main contractors for the construction of educational premises in Cambridge. The subcontract was agreed to be governed by a set of standard terms known as DOM/1. The subcontract works have achieved substantial completion, but the time and circumstances of Mellowes' performance of them is a matter of dispute.

2. Clause 21 of DOM/1 provides for a system of interim payments by the contractor, to be paid according to a set timetable and calculated by taking the then current gross valuation of the subcontract works and deducting any retention by the contractor permitted by clause 21.5 of DOM/1, and any set-off permitted by the restrictive provisions of clause 23, which require clear calculation and advance notice of any sum sought to be the subject of a set-off. By its Statement of Claim Mellowes claim some £88,000 as owing to them in respect of the alleged value of the subcontract works, taking into account a single sum of some £53,600 paid by Bell. The Official Referee has stayed the major part of the proceedings under the Arbitration Act. There is no appeal against that part of his order. Continuing before him, and before us, is Mellowes' application for summary judgment for what it says is its right to payment now in respect of an amount that must have been due under interim payments number 1 and 2, payable respectively on 13 August 1995 and 13 September 1995.

3. Shortly after the latter date, that is on 18 September 1995, a letter was furnished to Mellowes by Bell claiming various set-offs, which was accepted by Mellowes, at least for the purposes of the present Order 14 application, as having effectively asserted those set-offs under clause 23 against the obligation to make interim payments 3 and 4, which fell due after the date of 18 September 1995 letter. The effect of that letter on the claims made by Mellowes under interim payments 1 and 2 will have to be considered hereafter.

4. Mellowes' present claim under Order 14 is based on what it says was Bell's own valuation of Mellowes' work current at the date relevant to interim payment number 2. Mellowes drew that valuation from a document produced by Bell on 10 October 1995, from which Mr Lees, Mellowes' quantity surveyor, concluded that the gross value of Bell's valuation had been £75,745.41. After applying various contractual deductions, and giving credit for the £53,604.28 paid by Bell, Mr Lees concluded, and so swore in support of Mellowes' Order 14 application, that the sum owed to Mellowes on the basis of that valuation was £16,195.12. However, in its own evidence in the Order 14 application Bell demonstrated, and Mellowes now agrees, that the valuation had been wrongly understood by Mr Lees, and that the true figure for the gross valuation on which Mellowes' claim was based was £69,202.14. As a result, Mellowes reduced its claim before the Official Referee to the sum to be deduced from that revised valuation, that is to say £10,165.49. No further affidavit correcting the applicant's original affidavit or giving an explanation of the error has been filed. That the original sum was incorrectly claimed is the subject of a respondent's notice, asserting that to be a further ground why judgment should not be entered on Mellowes' summons. I revert to that matter at the end of this judgment.

5. Bell's letter of 18 September 1995 asserted serious additional costs incurred by reason of delay on the part of Mellowes, a complaint that was further substantiated in later correspondence. For the purposes of this application it is assumed that those assertions are correct or at least strongly arguable. The losses, if established, would be sufficient to extinguish the whole of Mellowes' claim, and not merely to extinguish that part of it that is the subject of this summons. The Official Referee held that those losses could not be asserted by way of set-off against the claim under the summons because of the provisions of clause 23.2 of the standard form contract. That clause, in its relevant parts, reads as follows: *"2 No set-off under [this clause] may be made unless such set-off has been quantified in detail and with reasonable accuracy by the Contractor; and the Contractor has given to the Sub-Contractor notice in writing specifying his intention to set- off the amount so quantified together with the details referred to above and the grounds on which such set-off is claimed to be made. Such notice shall be given not less than 3 days before the date upon which the payment from which the Contractor intends to make the set-off becomes due under [earlier provisions of the contract]."*

6. The notice of 18 September 1995 was not delivered before the required date of payment under the interim payment obligation. The Official Referee however held that that was not a barrier to the use of the claim in respect of delay as an arguable defence to the interim payment claim if the delay claim could be characterised not as a matter of set-off but as a matter of abatement, as first recognised in **Mondel v Steel** 8 M & W 858.

7. Bell seeks to maintain that conclusion in this appeal. It will be apparent that Bell is only driven to the law of abatement because, as is agreed between the parties, whilst reliance on anything characterised as "set-off" is precluded by the terms of clause 23, that clause does not exclude a defence or plea of abatement. That was made clear, for instance, in the case of **Acsim (Southern) v Danish Contracting and Development** 47 BLR 55 at p70 where Ralph Gibson LJ, with whom both Neill LJ and Slade LJ agreed on this point, held that a provision limiting "***set-off***" in terms similar to those adopted in our present clause 23 did not affect the right of a contractor to defend a claim for interim *payment "by showing that, by reason of the sub-contractor's breaches of contract, the value of the work is less than the sum claim claimed under the ordinary right of defence established in* ***Mondel v Steel*** *."*

8. Miss Randall, Counsel for Mellowes, did not question the existence of the defence of abatement. Her case was, rather, that the defence was bounded by strict limitations, and only available to Bell within those limitations. In particular, abatement was only available to assert claims that related to the physical value of the goods sold or works done, and not to assert, as Bell sought to do in this case, what might be called collateral losses caused by, in this case, delay in completing the works.

9. This argument as it applied to the present case was expressed by her in two propositions:
   (i) The defence of abatement could not be raised against a claim under a contract for work and materials when the defence consisted of complaints about delay in performing the works, as opposed to complaints about the quality or completion of the works.
   (ii) If the defence of abatement was available in principle, the amount of the abatement could not be calculated by the cost to the defendant of the delay, rather than by the effect on the "value" of the works themselves.

10. Although Miss Randall strongly urged that these are separate points, I for my part continue to think that, at least in the context of the present case, they really collapse into a single issue: because if the defence of abatement were to be available in a case of delay, even where the works had been completed satisfactorily in every other respect, the sum going in reduction of the plaintiff's claim can necessarily only be expressed in terms of the cost of that delay. It seems to me, therefore, that Miss Randall's second point is really an argument as to why it is difficult or inappropriate for the reduction in "value" which is said to be the essence of the defence of abatement of price to be applied in a case where the only complaint is of loss through delay; rather than being a reason for not applying the defence were it to be decided that it could apply in principle in the case of damages for delay.

11. This enquiry into the nature of the defence or claim of abatement necessarily starts with the account by Lord Wensleydale, Parke B as he then was, in Mondel v Steel 8 M&W at p 871. Parts of that account do indeed give support to a view that abatement applies to all matters of defence. Thus at page 870 Parke B said this: *"Formerly, it was the practice, where an action was brought for an agreed price of a specific chattel, sold with a warranty, or of work which was to be performed according to contract, to allow the plaintiff to recover the stipulated sum, leaving the defendant to a cross action for breach of the warranty or contract; in which action, as well the difference between the price contracted for and the real value of the articles or of the work done, as any consequential damage, might have been recovered;..."*

12. There is no suggestion that, when the defendant's interests became able to be asserted by abatement, what Parke B calls consequential damage dropped out of the reckoning. On this view, when Parke B summarised the nature of the defence at page 871 by saying: *"It must however be considered, that in all these cases of goods sold and delivered with a warranty, and work and labour, as well as the case of goods agreed to be supplied according to a contract, the rule which has been so found convenient is established; and that it is competent for the defendant, in all of those, not to set-off, by a proceeding in the nature of a cross action, the amount of damages which he has sustained by breach of contract, but simply to defend himself by shewing how much less the subject-matter of the action was worth, by reason of the breach of contract;..."*

13. It is arguable that he was by his reference to "the subject-matter of the action" (not, it will be noted, of the articles or works) admitting to the defence of abatement any claim legitimately arising from the contract on which the plaintiff sued; and not limiting the subject-matter of the action to the works themselves which, as Counsel for the appellant pointed out, were not rendered of less worth by reason simply of delay.

14. To hold that the defence of abatement has that general reach would not be inconsistent with the upholding by the House of Lords in The Aries [1977] 1 W.L.R. 185 of the rule that abatement does not apply to obligations to pay freight: see in particular the judgment of Lord Simon of Glaisdale at page 193B, who regarded freight as an atypical survivor of a world transformed by what his Lordship described as "the new general common law rule" of Mondel v Steel . That however leaves to be decided what the contents and limits of that rule in fact are; and whether in Mondel v Steel the rule was intended to have the general reach that might be thought to be indicated by the passages I have so far cited. I am persuaded that the defence does not have the general reach contended for by the respondents, and in particular does not include claims that as in the present case assert losses attributable solely to delay. My reasons for so thinking are as follows.

15. First, that Mondel v Steel is limited in its effect is plain from the case itself. The short issue was whether, when a buyer had pleaded breach of warranty in defence of an action for the price of the goods, he could thereafter maintain his own action for the further cost of repairs occasioned by the breach. Parke B held that he could, because what we would now call the Mondel v Steel abatement in the claimed value of the goods on the one hand, and the claim for the cost of extra work on the other hand, were different in their legal nature. As he said, at page 872: *"... all the plaintiff could by law be allowed in diminution of damages, on the former trial, was a deduction from the agreed price, according to the difference, at the time of the delivery, between the ship as she was, and what she ought to have been according to the contract: but all claim for damages beyond that, on account of the subsequent necessity for more extensive repairs, could not have been allowed in the former action, and may now be recovered."*

16. Secondly, **Mondel v Steel** was understood in that sense by a strong Court of Queens Bench in the case of **Davis v Hedges** [1871] LR 6 QB 687. The issue was whether **Mondel v Steel** required, as opposed to permitted, the employer under a building contract to deploy his complaints as a defence to an action for the price of the works. Speaking for Blackburn J and himself, Hannen J held that it did not, in the course of his judgment remarking, at page 691, that: *"The cases are perhaps rare in which the consequences of defective performance of work are limited to the depreciation of the value of the work done; they usually involved consequential damage by reason of the necessity of repairing the defective work; and for this the case of **Mondel v Steel** decides a separate action must be brought. Parke B there says...."* and Hannen J then cited the passage from **Mondel v Steel** that I have ventured to set out immediately above.

17. Third, the industry of Miss Randall took us to **Oastler v Pound** [1863] LT(ns) 852. This case, though very little remarked in the 130 years during which it has stood, was, again, decided by Judges of the very highest eminence. The defendant guaranteed the performance by a third party of a contract for goods to be supplied by the plaintiff to that third party. Amongst other defences, it was argued that the plaintiff's delay in delivery provided a defence to the third party, and thus to the defendant guarantor. Counsel argued that any breach of contract entitled the other party to set-off, only to be met by the intervention by Blackburn J that: *"any other damage than the difference in the value of the thing itself is a cross-action"*, a conclusion, specifically distinguishing **Mondel v Steel** , that he confirmed in his judgment. Mellor J specifically agreed, saying: *"There is a manifest distinction between **Mondel v Steel** and this case, where it is sought to set off damages for delay."*

18. That, it will be seen, is the very contention of the appellant before us. It seems to be clearly consistent with the restricted view of **Mondel v Steel** that Blackburn J subsequently supported in **Davis v Hedges . Oastler v Pound** may not, strictly, bind us, but I for my part would need very strong persuasion that an unchallenged decision of such a court was wrong before I declined to follow it. In fact, however, **Oastler v Pound** clearly fits into what appears to have been Lord Wensleydale's own view of **Mondel v Steel** , as the approach to that latter case in **Davis v Hedges** further demonstrates.

19. Fourth, Miss Randall can gain some support from **Acsim (Southern) Ltd v Danish Contracting and Development Co Ltd** 47 BLR 55, to which I have already alluded in another context. I do not think that the Court of Appeal there directly addressed the specific question in issue here, and I am therefore not able to accept the case as binding authority on our present point. However, in analysing the various matters of complaint raised in that case the Court of Appeal accepted that complaints of delay were a matter of set-off, and thus vulnerable to the operation of a clause substantially to the same effect as our own clause 23, but that that did not affect complaints (and I quote here from Slade LJ at page 80): *"that the work for which the claim for interim payment was demanded has not been properly executed, by way of defence in accordance with the principles recognised by Lord Diplock in* ***Modern Engineering v Gilbert-Ash*** *[1974] AC 689 at page 717."*

20. That analysis is, at the very lowest, not inconsistent with the case that Miss Randall puts before us.

21. Fifth, Miss Randall pointed out that the principles recognised by Lord Diplock in Gilbert Ash included the long-recognised restriction of abatement to contracts for sale of goods and for work and labour. Why, she asked rhetorically, should that be, if any defence of any sort can be brought within the ambit of abatement? If damages for delay, as opposed to reductions in the value of the goods or works, can be the subject of abatement, why should that not be so in, for instance, all contracts for services and not just in contracts for work and labour.

22. Sixth, in **The Brede** [1974] 1 QB 233 at 248D Lord Denning MR contrasted a claim for defective work with the case where: *"the cross-claim does not reduce the* ***value*** *of the goods sold or the work done, but causes other damage; such as cases where goods are delayed in delivery and the buyer has a cross-claim for delay; or where a contractor who is employed to clean windows negligently breaks the leg of a chair. In former times such damages could only be claimed in a separate action: see* ***Mondel v Steel*** *8 M&W 858, 870-872, and would no doubt be subject to a time-bar, where appropriate. Since the Judicature Act 1973 [sic], however, these damages can be set up by way of an equitable set off in diminution or extinction of the claim - leaving any over-plus to be the subject of a counterclaim."*

23. I respectfully consider that that statement accurately sets out the limits of the rule of abatement in **Mondel v Steel** , as demonstrated by the earlier authority that I have ventured to cite. That rule does not apply to claims based on delay. I do not see any oddity or inconvenience in that. The difference between abatement and set-off is only of significance in very particular situations, namely special issues of limitation, such as was the case in **The Brede** and **The Aries** ; or where, as in our case, a contractual limitation on remedies confines itself to "***set-off***".

24. The historical limits on abatement do not, in the normal case, in any way affect the ultimate rights of a party, any more than in our case they in law affect the ultimate rights of Bell; because, as Lord Denning MR says in the passage that I have just ventured to cite from **The Brede** , those rights will in any event normally be able to be asserted by set-off. And I would say further that although **The Aries**_was concerned with the special issue of the application of abatement to freight, and therefore does not directly affect the issue before us, the speeches of their Lordships in that case at least strongly suggest that we are not free to depart, and should not depart, from the established limits and ambit of the defence of abatement.

25. I hold, therefore, the defence asserted in this case is not available to Bell, and judgment should be entered against them.

26. I am not deflected from that conclusion by the issue raised in Bell's respondent's notice. It is freely agreed that the issue is one of procedure, not of substance. When the error as to quantum was pointed out to it, Mellowes simply limited its claim in circumstances that were wholly obvious to, and which in no way misled or threaten to mislead, either Bell or the court. The case is quite different from **Barclays Bank v Piper** , relied on by Bell, where the affidavit did not comply with Order 41 r5(2), and where there was or might have been genuine doubt as to the substance and basis of the applicant's case.

27. Nevertheless, I would not wish to undermine the importance of complying with the procedural requirements of Order 14, involving as that order does a stringent and unusual jurisdiction. But in this case those requirements in my view were in fact complied with. The affidavit was in proper form, and

correctly deposed to the fact that there was no defence to the claim. If subsequently it became apparent that the claim was of less monetary value than originally asserted, I cannot see that that renders the original affidavit defective or in need of correction. I would allow this appeal.

LORD JUSTICE HOBHOUSE:

28. I agree that this appeal should be allowed for the reasons given by Buxton LJ. There is very little that I wish to add.

29. The issue on this appeal arises from the distinction between the common law defence of abatement and the defence of equitable set-off. Under the DOM/1 form of sub-contract, the right of the main contractor to make a set-off against the sums otherwise payable to the subcontractor is subject to the conditions set out in clause 23 of the form. The main contractor's right to raise an equitable set-off is regulated by the clause but the clause does not affect the right of the main contractor to exercise any right he may have of common law abatement **(Gilbert Ash v Modern Engineer** [1974] AC 689 at 718 per Lord Diplock; **Acsim v Danish Contracting** (1989) 47 BLR 55).

30. By the middle of the last century both types of defence were clearly established. The judgment of Lord Cottingham, LC in **Rawson v Samuel** (1841) Cr & Ph 161 had defined the principles governing the entitlement to claim an equitable set-off. In **Mondel v Steel** (1841) 8 M&B 858 Parke B had explained the character and scope of the right to abate the price payable for goods supplied or work done. The two types of defence were described by Lord Denning MR in **Henriksens Rederi A/S v Rolimpex** [1974] 1 QB 233 at 247.

"Our law has divided cross claims (which arise out of the same transaction as the claim) into two categories: First: when the cross claim goes directly in diminution or extinction of the claim such as cases where goods are sold with a warranty and by reason of the breach of warranty the profits are worth less than the contract price; or, cases where work and labour are expended on a building and, by reason of defects, the work actually done is worth less than the contract price.

In every such case it is plain that the plaintiff, not having completed the agreed work in accordance with the contract, is not entitled to the whole of the agreed sum. He ought not, therefore, to recover judgment for that sum but only for the lesser sum. ... ...

*Secondly: when the cross claim does not reduce the value of the goods sold or the work done, but causes other damage; such as cases where goods are delayed in delivery and the buyer has a cross claim for damages for delay; or where a contractor is employed to clean windows and negligently breaks the leg of a chair. In former times such damages could only be claimed in the separate action: see **Mondel v Steel** and would no doubt be subject to a time bar where appropriate. Since the Judicature Act 1873, however, these damages can be set up by way of an equitable set-off in diminution or extinction of the claim - leaving an over-plus to be the subject of a counter-claim. ... It is available whenever the cross claim arises out of the same transaction as the claim; or our of a transaction which is closely related to the claim."*

31. The contrast is between those failures to perform the contract which "***directly***" reduce the *value* of the thing itself as opposed to breaches which have caused the relevant party loss and give rise to cross-claims which he is allowed to set off. Lord Denning gives as an example of the latter category where goods are delayed in delivery and the buyer has a cross-claim for damages or delay.

32. The distinction between equitable set-off and abatement and the limited character of the right of abatement clearly appear from **Mondel v Steel** (which was a shipbuilding case) and two succeeding cases. In **Mondel v Steel** at page 871 Parke B referred to the fact that a defendant was entitled "*to show that the chattel by reason of the non-compliance with the warranty in the one case and the work in consequence of the non-performance of the contract on the other were diminished in value*". He said: "*It must however be considered that in all these cases of goods sold and delivered with a warranty and work and labour as well as the case of goods agreed to be supplied according to a contract, the rule which has been found so convenient is established; and that it is competent for the defendant in all of those, not to set-off, by a proceeding in the nature of the cross action, the amount of damages which he has sustained by breach of the contract, but simply to defend himself by showing how much less the subject matter of the action was worth by reason of the breach of contract; and to the extent that he obtains, or is capable of obtaining, an abatement of price on that account, he must be*

considered as having received satisfaction for the breach of contract, and is precluded from recovering in another action to that extent; but no more."

33. Thus, the right to an abatement was the right to deduct *"from the agreed price according to the difference, at the time of delivery, between the ship as she was and what she ought to have been according to the contract".*

34. In **Oastler v Pound** (1863) 7 LTNS 852 the question was whether delay in the performance of a contract for the supply of goods gave rise to a common law right to abate the price payable for those goods. When it was argued that it did, Blackburn J responded: *"Any other damage than the difference in value of the thing itself is the subject of a cross action."*

35. In their judgments both members of the Court, Blackburn J and Mellor J, distinguished the case of damages for delay in the supply of goods from the right of abatement and the decision in **Mondel v Steel**.

36. In **Davis v Hedges** (1871) LR 6 QB 687 Hannen J giving the judgment of himself and Blackburn J followed and applied **Mondel v Steel** and in doing so contrasted *"depreciation of the value of the work done"* with *"consequential damage".*

37. It is therefore clear that, for a party to be able to rely upon the common law right to abate the price which he pays for goods supplied or work done, he must be able to assert that the breach of contract has directly affected and reduced the actual value of the goods or work - "the thing itself". In other words any other loss or damage, if it is to be relied upon by way of answer to a claim for the price, has to arise from the principle of equitable set-off. In most contractual relationships there would be no need to draw a distinction between the two types of defence. But under DOM/1 it is necessary to do so.

38. Whilst it may be possible to conceive of a case in which delay has affected the value of the thing itself, the normal effect of breaches of the obligation of timeous performance will be to cause losses to the other contracting party which are consequential upon that breach and therefore can only be relied upon, if at all, under the principle of equitable set-off. In the present case the factual situation is clear. The plaintiff sub-contractor's claim to be paid the price is based upon the valuation of the goods supplied and work done. Indeed the valuation was the defendant main contractor's own valuation, and is undisputed. The case of the defendants is that the plaintiffs' delays caused them serious losses through the prolongation of the head contract, the disruption of their own contractual works and those of other sub-contractors, the need to accelerate other work, and the reduced contribution to their own overhead expenses. Thus, the defendants' case is based upon financial losses which they say they have suffered as a consequence of the plaintiffs' breaches of their obligations of timeous performance. Subject to the terms of Clause 23, those losses can be relied upon to support an equitable set-off but they cannot justify the legal defence of abatement of the price.

39. This conclusion is in line with the views expressed by the Court of Appeal in the case of **Acsim**. There Ralph Gibson LJ at page 67 and Slade LJ at page 80 expressly agreed with the decision of Judge Hawser QC and the concession of counsel that losses suffered as a result of delay in the performance of the contract could not be relied upon to abate the price payable.

40. There is no substance in the defendants' point under RSC Order 14 r2. The requirements of that rule were satisfied.

41. Accordingly in agreement with Buxton LJ and the reasons which he has given, I do consider that this appeal should be allowed.

LADY JUSTICE BUTLER-SLOSS: I agree with both judgments.

Order: Appeal allowed; paragraphs 3 and 5 of the order of His Honour Judge Wilcox varied and in substitution for paragraph 3 there will be summary judgment to the appellant plaintiff in the sum of £11,944.45 together with interest in the sum of £1,999.06; half the costs of the hearing below will be paid by the respondents to the appellants; appellants to receive their costs of the appeal; application for a stay refused.

MISS LOUISE RANDALL (Instructed by Neil F. Jones & Co., Birmingham, B15 1BQ) appeared on behalf of the Appellant
MR S HENDERSON (Instructed by Fenwick Elliott, 353 Strand, London, WC2R OHS) appeared on behalf of the Respondent