Skanska Rashleigh Weatherfoil Ltd v Somerfield Stores Ltd [2006] ABC.L.R. 11/22

CA on appeal from QBD (Mr Justice Ramsey) before Neuberger LJ; Richards LJ; Leveson LJ. 22nd November 2006

LORD JUSTICE NEUBERGER:

1. This is an appeal from the decision of Ramsey J on the preliminary point of interpretation of a contract in a letter dated 17 August 2000 (the "August letter"), which included a temporary arrangement between Skanska Rashleigh Weatherfoil Ltd ("Skanska") and Somerfield Stores Ltd ("Somerfield").

2. Somerfield is a well-known operator of around 1300 supermarkets in the United Kingdom. In 2000 it decided to reorganise the way in which it procured the maintenance of those buildings and the machinery therein. It had in mind either a single national contract or a limited number of regionally-based contracts. Such a contract is known as a Facilities Management Agreement ("FMA").

3. On 19 June 2000 Somerfield invited Skanska, which specialises in such services, to tender for the provision of maintenance services to its properties in four, subsequently reduced to three, regions. The letter (the "June letter") included a draft of the proposed contract in the form of the incomplete FMA which, although in draft form, I shall call "the June FMA". The June letter invited prices to be submitted on the basis of three different service levels, of which only one, the "fully comprehensive level", is relevant.

4. The basic nature of the proposed FMA was that a contractor, for instance Skanska, would be required to provide preventative and reactive maintenance services to all the properties in the region for a term of three years. Preventative maintenance was envisaged as involving visits to carry out regular maintenance and servicing and, where necessary, replacements in accordance with a schedule to be agreed. Reactive maintenance was envisaged as being *ad hoc* maintenance, for instance carrying out work on request caused by acts of vandalism or leaking pipes. The June FMA contemplated a fixed annual fee, payable by instalments, for preventative maintenance services, and payment at agreed hourly rates for the reactive maintenance services.

5. Between June and August 2000, discussions between Skanska and Somerfield took place as to the scope and terms of the ultimate FMA they would enter into. Skanska submitted a tender on 14 July 2000, which was revised in a number of respects in the next month. By mid-August 2000 the position was as follows. There was an incomplete draft of the proposed FMA, namely the June FMA, which if finalised would govern the relationship between the parties for some three years. Pursuant to Somerfield's request, Skanska submitted its tender, which had been subjected to a number of revisions and was itself subject to a number of negotiations. The parties accordingly envisaged that there would have to be further negotiations before the June FMA, as amended by agreement, could or would eventuate into a contract.

6. However, Somerfield wanted to receive the provision of maintenance services immediately. In those circumstances Somerfield wrote a letter to Skanska on 17 August 2000. The letter was headed "Subject To Contract" and was in the following terms, save that the paragraphs were un-numbered, but I have numbered them for ease of reference:

   "Dear Sirs,

   Facilities Management Agreement

   1. *We refer to the invitation to tender ("Tender") sent to you on 19th June 2000 for the provision to us of preventative and reactive maintenance services ("Services") in, respect of the major plant and related equipment. located in our stores in regions two (2) six (6) and eight (8) as detailed in the Tender.*
   2. *We now wish to appoint you to provide us with the Services, which are more particularly described in the contract (ref.: JRB/2240842 DRAFT 3 - 14th June 2000) ("Contract") enclosed with the Tender.*
   3. *This appointment is, however, strictly subject to contract, and to the approval of our board. As soon as this letter has been signed, we both undertake to commence good faith negotiations with a view to completing and signing a mutually acceptable contract derailing the terms of your appointment as soon as is reasonably practicable ("the Agreement"). No commitment from either of us relating to the provision of the Services shall (subject to the remaining provisions of this letter) arise until we have both signed the Agreement*
   4. *We agree to negotiate exclusively with you in respect of the Services until we give you notice indicating otherwise, save that we may negotiate the termination of our existing arrangements with our existing suppliers relating to the provision of any services similar to the Services.*
   5. *In consideration of the above, and whilst we am negotiating the terms of the Agreement, you will provide the Services under the terms of the Contract from 28th August 2000 (or such other date as we may advise to you) until 27th October 2000 ("the Initial Period"), such Services to be provided at the prices detailed in the Tender return provided by you (as subsequently amended) as the same are more particularly itemised on the attached schedule.*
   6. *In agreeing to the Services being provided on the above basis during the Initial Period, neither of us is in any way fettering our discretion to seek additional or different provisions or prices when negotiating the detailed terms of the Agreement. We acknowledge that you will be expending time, resources and expense during the Initial Period, and in preparing to provide the Services after the Initial Period. Such expenses will include staff recruitment and the purchase of equipment. We, therefore, agree to reimburse your reasonable wasted costs and expenses should the Agreement not be signed or should we unilaterally withdraw from, or otherwise terminate, negotiations prior to signature of the Agreement PROVIDED ALWAYS that our liability under this paragraph shall not in any event exceed ..."*

The August letter ended by inviting Skanska to confirm its acceptance of its terms by countersigning and returning a copy to Somerfield.

7. On 21 August 2000, Skanska returned a copy of the letter, duly countersigned "agreeing to the terms set out above". On the same day Skanska also replied to the rest of the August letter in relation to the projected, longer term, three-year arrangement. In that letter various points were made by Skanska, including the point that it wished to limit its liability under an indemnity in the June FMA to £10 million in any one year.

8. It is common ground that the August letter, although headed "subject to contract", did include a contract relating to the provision of "services", as defined in paragraphs 1 and 2, for the "initial period" as defined in paragraph 5. (Any doubt about this must be put to rest by the bracketed words towards the end of paragraph 3). I shall call this contract "the temporary arrangement".

9. Although there were other preliminary issues which were determined by Ramsey J, the only issue which is the subject of this appeal is whether the temporary agreement included most of the terms of the June FMA, referred to as the "contract" in paragraph 2 therein, or whether it only incorporated very few of them.

10. Identifying the issue in this way is self-evidently not entirely satisfactory because of its lack of specificity. As I understand it, before the arguments were orally developed before the judge, the position each party took was rather more extreme than the position it now takes. Skanska was originally contending that none of the terms of the June FMA were to be implied in the temporary arrangement; the only purpose of referring to the June FMA in paragraphs 2 and 5 of the August letter was, on its case, to identify the nature of the works performed under the temporary arrangement. Somerfield, on the other hand, originally contended that all the terms of the June FMA were incorporated into the temporary arrangement, particularly in light of the way in which the June FMA was referred to in paragraph 5 of the August letter. However, the position of each party mellowed somewhat during the hearing and they both approached the issue "in terms of broad principle" as the judge recorded in paragraph 69 of his judgment.

11. Because neither party had an entirely clear position on every provision of the June FMA, the judge expressed his conclusion in this way in the next paragraph of his judgment: *"As a result, I answer this issue in terms of the broad principle that the terms incorporated are those terms of the June FMA limited to terms necessary to define the services which Skanska was to provide but also, as I have set out above, I have identified certain [broad] terms taking account of the limited submissions made as to the practical effect of that broad principle."*

12. In effect, therefore, the judge accepted Skanska's submission that very few of the provisions of the June FMA, in effect only those which directly or indirectly defined "the services", were to be treated as incorporated into the temporary arrangement. Concomitantly he rejected Somerfield's submission that the temporary arrangement incorporated all the provisions of the June FMA, save those which were inconsistent with the terms of the August letter or with a two-month agreement. In reaching his conclusion the judge directed himself in accordance with the approach set out by Lord Hoffman in ***Mannai Investment Co v Eagle Star Life Assurance*** [1997] AC 749-775, and in ***Investors Compensations Scheme v West Bromwich Building Society*** [1998] 1 WLR 912-914. In other words, in summary, he sought to interpret the words of the August letter as they would be objectively be understood against the background of the particular context in which they were written.

13. The judge first considered the words of the August letter and, in particular, the reference to the June FMA, described therein as the "contract" in paragraphs 2 and 5 of that letter. He considered that the wording in each case was consistent with the notion that the June FMA was simply being referred to for the purpose of identifying "the services" which Skanska was to provide during the period specified in paragraph 5.

14. Turning to the surrounding circumstances, the judge thought that two factors were of particular importance in relation to the issue of whether the temporary arrangement was to be treated as subject to most of the terms of the June FMA. First, he considered that the June FMA was intended to apply for a reasonably long period, namely three years, whereas the temporary arrangement was intended to be for a much shorter period, namely two months, although it is fair to say that, in practice, due to extensions agreed expressly or impliedly between the parties, it lasted much longer than that. Secondly, he considered that it was clear from the terms of the August letter that the one thing that the parties had yet to agree, and were anxious not to agree for the moment, was whether they should be bound by all the terms of the June FMA. It was those terms that they were seeking to negotiate, and it was because they had not reached agreement as to all those terms, that they had not reached a binding agreement there and then. Accordingly, he thought it highly unlikely that the parties would have intended to have been bound by the June FMA.

15. Like many issues of interpretation, the point raised in the instant case is not entirely easy and it was rendered more difficult by the change of position on the part of each party during the hearing. That is not intended to imply any criticism of a party who changes its position in relation to a point of interpretation or any other point of law during argument in court. One of the many benefits of such oral debate is it enables points to be refined or improved in the way which would be hard or even impossible if the debate were pursued solely in writing.

16. I turn to paragraph 2 of the August letter. It seems to me that the reference there to the June FMA is quite plainly limited in the way that Skanska argues and the judge held. The purpose of the reference to the June FMA was merely an order to identify "the services" there described. Indeed, I do not understand Somerfield to argue the contrary.

17. Where I think Skanska's argument faces more difficulty is when one turns to the reference to the June FMA in paragraph 5. Under that paragraph, Somerfield proposed, and Skanska agreed, that Skanska would "provide the services under the terms of the Contract". Reading that phrase on its own at least, it seems to me the natural meaning of the expression, particularly in light of the words that I have emphasised, is that the terms of "the contract", that is the June FMA, will govern the terms upon which the services are to be provided under the temporary arrangement. Although an arrangement that one party will provide to the other "the services under the terms of the contract" could be capable of being limited to identifying the services by reference to the contract, I am firmly of the opinion that that is not the natural or primary meaning the words convey to an ordinary speaker of English, whether a lay person, a businessman or a lawyer. It is not irrelevant to mention that, as I see it, the words "the terms of" would be redundant if what was meant was simply the services as described or identified in the contract.

18. It is, of course, very dangerous to construe an expression in isolation. It is trite law that a word or expression used in a contract has to be construed in its overall context. That is the point made in the two cases referred to earlier. This, of course, means that one has to take into account the other provisions of the August letter and the surrounding circumstances in commercial commonsense.

19. It seems to me that if one turns to paragraph 2 of the August letter, the natural and primary meaning of the centrally significant word in paragraph 5 is reinforced. That is for two reasons. First, in paragraph 2, the reference to the June FMA was much more limited. As I have indicated, the language used was intended to invoke the June FMA merely in order to identify the services referred to. In other words, the contrast between the way in which the services in the June FMA are linked in paragraph 2 and the way in which they are linked in paragraph 5 reinforces an interpretation which accords with what I consider to be the primary meaning of the word in the latter paragraph.

20. Secondly, given that, in paragraph 2 of the August letter, "the services" have already been clearly defined by reference to the June FMA, it is difficult to see as Skanska's case why there is reference again to the June FMA in connection with the services in paragraph 5. The only purpose in that latter paragraph was, as Skanska argues, to identify the nature of the services by reference to the June FMA. Accordingly, in my judgment, at least if one confines oneself to the terms in which the August letter is expressed, it seems to me that it bears Somerfield's interpretation much more satisfactorily than it bears that of Skanska.

21. As already mentioned, the interpretation of the provision in the commercial contract is not to be assessed purely by reference to the words the parties have used within the four corners of the contract, but must be construed also by reference to the factual circumstances of commercial common sense. However, it seems to me right to emphasise that the surrounding circumstances and commercial common sense do not represent a licence to the court to re-write a contract merely because its terms seem somewhat unexpected, a little unreasonable, or not commercially very wise. The contract will contain the words the parties have chosen to use in order to identify their contractual rights and obligations. At least between them, they have control over the words they use and what they agree, and in that respect the words of the written contract are different from the surrounding circumstances or commercial common sense which the parties cannot control, at least to the same extent.

22. Particularly in these circumstances, it seems to me that the court must be careful before departing from the natural meaning of the provision in the contract merely because it may conflict with its notions of commercial common sense of what the parties may must or should have thought or intended. Judges are not always the most commercially-minded, let alone the most commercially experienced, of people, and should, I think, avoid arrogating to themselves overconfidently the role of arbiter of commercial reasonableness or likelihood. Of course, in many cases, the commercial common sense of a particular interpretation, either because of the peculiar circumstances of the case or because of more general considerations, is clear. Furthermore, sometimes it is plainly justified to depart from the primary meaning of words and given them what might, on the face of it, appear to be a strained meaning, for instance where the primary meaning of the words leads to a plainly ridiculous or unreasonable result.

23. I have already referred to the two external commercial factors which weighed with the judge when deciding to adopt Skanska's approach to the construction of paragraph 5 of the August letter. They were: a) the fact that the parties did not want to be bound by the terms of the June FMA; and b) the fact that the June FMA, if executed, would have lasted for some three years, whereas the temporary agreement was only intended to be for a term of two months.

24. With due respect to the judge, it seems to me that whether one takes those points together or separately, they do not establish, or even really support, the conclusion that he reached. The parties wished to negotiate about the terms of the June FMA because they did not want to commit themselves to its precise terms for some three years, but this does not mean that they were not prepared to be bound by those precise terms over a short two-month period while the negotiations continued and, hopefully, eventuated into a contract. Accordingly, it appears to me that, contrary to the opinion of the judge, the fact that the parties were not prepared to be bound by the June FMA for a period of three years does not mean that they were not prepared to be bound by it for a much shorter period while they sorted out their longer term agreement. In my judgment, this conclusion is reinforced by the fact that as the negotiations which were going on between the parties at the time of the August letter show, they clearly thought that the June FMA provided a good basis for negotiations as to the terms which would apply for three years, ie that they were content with its general thrust.

25. If one accepts that, it seems to me that it is perfectly possible that the parties would have agreed that the June FMA would apply to the short two-month period, contemplated by paragraph 5 of the August letter, rather than leaving it open to argument as to what terms, if any, were to be implied into the arrangements between them for that short period. Thus, the June FMA contained detailed provisions with regard to payment and consequences of determination, at least some of which would plainly be sensible to have implied into a contract for the provision of the "services", even for as short a period as two months.

26. I think that point is somewhat reinforced when one bears in mind the relatively complex nature of the services, as Mr Jeremy Nicholson QC, who appears with Mr Adrian Hughes QC, for Somerfield, contends. The services were of a relatively complex nature, including over three hundred different types of operation, many of them involving specialist expertise, for instance those services extending, for instance, to lift and refrigeration systems. It appears to me more likely than not that the parties would have expected to have fairly detailed provisions, such as those contained in the June FMA, rather than virtually no express terms, as Skanska's case seems to involve, governing their relationship even under the temporary agreement.

27. Mr Stephen Dennison QC, who appears with Miss Serena Cheng for Skanska, raises a number of further points in his excellent submissions in support of the judge's conclusion. His first point is that there are terms of the June FMA which are inconsistent with the terms of the August letter or with a two-month, as opposed to a three-year, agreement. In my opinion, the answer to that is that any such terms are simply not included in the temporary agreement. I appreciate that this conclusion can be said to involve implying something into paragraph 5 of the August letter but that causes me no concerns. It would be classic case for implication, though requirements of both obviousness and necessity are plainly satisfied. Such an approach to a corporation is supported by the House of Lords in ***Thomas (TW) and Co Ltd v Portsea Steam Ship*** [1912] AC 1, and in the Court of Appeal in ***Hamilton and Co v Mackie and Sons*** [1889] 5 Times Law Report 677 and ***Modern Building Wales Ltd v Limmer Trinidad Ltd*** [1975] 1 WLR 1281, as discussed in Lewison J's book on Interpretation of Contracts (2004), pages 66-7.

28. I also accept that there could be arguments whether two or three of the terms of the June FMA are excluded. However, it seems to me that, apart from departing from the natural meaning of the centrally relevant words of the August letter, Skanska's interpretation would involve a requirement for implied terms which would very probably carry with it more room for argument than Somerfield's interpretation. If all that the parties had agreed was the services to be provided and prices, it appears to me almost self-evident that it would have been open house for both parties to argue about the terms to be implied, especially against the backdrop of the contractual negotiations.

29. Mr Dennison also relies on two reasons which emerged from the evidence before the judge as to why Somerfield may not have been prepared to agree a contract on the terms of the June FMA for three years as applying equally to a two-month period. Those reasons cannot, in my view, be relied on because of the simple fact that neither of those two reasons were known to Skanska at the time. It is only fair to add that I would not have found either of the reasons convincing in any event.

30. Mr Dennison also refers to the fact that, on the very day that Somerfield now says that the parties became bound by the June FMA, Skanska, having unlimited liability under its own indemnity therein, was saying to Somerfield that it was not prepared to have such an unlimited guarantee. This, in my view, is explained by the fact that Skanska was not prepared to take a risk for three years which it was prepared to take for two months.

31. The written submissions put before us by each party have been fairly extensive and I found both skeleton arguments helpful and impressive. However, it does not appear to me that there are any other points of significance which bear on the issue which we have to decide. In other words, I think the judge extracted the main relevant factors and set them out in his admirably clear judgment, although I have reached a different conclusion from him in what is not a wholly easy case and which, as with many interpretation issues, is to an extent a matter of impression.

32. Notwithstanding the benefit of all the guidance from the House of Lords and all the arguments of counsel, the natural meaning which the words in question convey to a particular reader, whether or not a judge, must inevitably play a very significant part in his or her decision as to that effect. In the end, in this case, the central point is the natural meaning of the words "you will provide the services under the terms of the contract" in paragraph 5 of the August letter. The natural meaning is reinforced by the wording of paragraph 2 of the letter and to put it at its lowest, it is not called into question by the surrounding circumstances or commercial commonsense.

33. In the circumstances, on the assumption that Richards and Leveson LJJ agree, the right course to take would be to allow the appeal and to remit the matter back to the judge as has been suggested on behalf of Skanska. The reason for remitting it to the judge is to enable him to decide which of the terms of the June FMA do indeed apply to the temporary arrangement. Clearly, there will be some terms of the June FMA which were inconsistent with the temporary arrangement. Given that this is an appellate court, the judge anticipated he would be deciding which of the terms of the June FMA were to be incorporated into the temporary arrangement and that aspects of this issue may turn on the evidence which the judge heard, I do not think it sensible for us to decide this point.

34. Accordingly, for my part I would allow the appeal and remit the matter to the judge in order for him to decide, if the parties are unable to agree, as to which of the terms of the June FMA do not apply to the temporary arrangement.

LORD JUSTICE RICHARDS:

35. I agree.

LORD JUSTICE LEVESON:

36. I agree both with the reasons and conclusions of my Lord, Lord Justice Neuberger, and his proposal for the disposal of this appeal.

Order: Appeal allowed.

MR J NICHOLSON QC & MR A HUGHES QC (instructed by Messrs Clarke Willmott) appeared on behalf of the Appellant.
MR S DENNISON QC & MS S CHENG (instructed by Skanska UK plc Legal Department) appeared on behalf of the Respondent.