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Insights

SAVED BY SILENCE: LETTERS OF INTENT AND ARCADIS V AMEC

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Employers under construction contracts often find themselves under time pressure to get started with construction of their projects prior to concluding negotiations with their preferred contractor and before the building contract is entered into. In such a scenario, employers commonly choose to rely on a letter of intent. This should give the contractor comfort to proceed with certain elements of the construction works, while the parties continue to negotiate the full contract terms.

Unfortunately not all "letters of intent" are clearly formulated in advance, and the parties may find themselves proceeding with the works on the basis of a series of exchanges and correspondence, as was the case in *Arcadis Consulting (UK) Ltd v AMEC (BSC) Ltd*.

The Court of Appeal overturned Coulson J's (as he then was) *first instance decision* in this case and held that the contract between Arcadis and AMEC **did** incorporate a term limiting Arcadis' liability for defective design. Coulson J had found that Arcadis' liability was unlimited, such that it was exposed to a potential loss of some £40 million, as opposed to liability capped at approximately £600,000.

Background

Amec was the specialist concrete sub-contractor on two large projects, the Wellcome Building and Castlepoint car park, and engaged Arcadis to carry out certain design works in connection with those projects in anticipation of a wider agreement between the parties.

On 8 November 2001, Amec sent Arcadis various documents, including a draft protocol agreement and terms and conditions that included a cap on Arcadis' liability (November Terms). The draft protocol agreement was an overarching "umbrella" agreement intended to govern various projects between the parties. It envisaged separate schedules and work instructions for each specific contract, but that each separate contract would be carried out pursuant to the same general terms and conditions. Amec instructed Arcadis to commence work in relation to the Wellcome Building on the basis of the November Terms, which Arcadis duly did.

On 6 March 2002, Amec sent Arcadis a letter of instruction in relation to the Castlepoint project, stating that the works were to be carried out in accordance with the terms and conditions "that we are currently working under". Without expressly agreeing to the terms and conditions, Arcadis acknowledged receipt of the letter on 8 March 2002, and on 22 March 2002 wrote back noting that certain matters still needed to be agreed for incorporation into the formal contract.

Following performance of Arcadis' services and completion of the works, the car park was alleged to be defective. Arcadis denied liability for the defects and sought a declaration that its liability was capped in accordance with the November Terms.

The TCC held that the parties had entered into a simple contract based on the letter of instruction of 6 March 2002. Coulson J concluded that none of the terms and conditions that had been exchanged between the parties in November 2001, or subsequently in January 2002 and March 2002, all of which included a cap on Arcadis' liability, had been incorporated into the contract as they had not been accepted by Arcadis.

The binding nature of an "if" contract

A letter of instruction may amount to a standing offer and, if accepted, will constitute a binding contract. This was referred to as an "if" contract in *British Steel Corp v Cleveland Bridge & Engineering Co Ltd*. It was found both at first instance and on appeal that, while Arcadis' letters of 8 and 22 March 2002 could stand as valid acceptance of Amec's standing offer in its letter of instruction, the strongest evidence of acceptance was Arcadis' conduct in undertaking the design work directed under that letter.

The Court of Appeal then went on to decide what were the terms of this binding contract. In other words, what were the terms and conditions that the parties were "currently working under". It concluded that the TCC failed to distinguish between the interim contract under which the parties were currently working and the final contract, the terms of which would supersede the interim contract once agreed. On the evidence, the Court of Appeal concluded that:

- The parties had agreed the November Terms, albeit in relation to the Wellcome Building.
- The November Terms created an interim contract that applied to all projects, including Castlepoint, until the final contract was agreed.
- These were the terms and conditions that the parties were "currently working under" and to which the March 2002 letter of instruction referred.

While acknowledging that there were outstanding matters of difference between the parties on the November Terms, the Court of Appeal concluded that these were not major differences and they did not prevent the parties from agreeing to them for the purpose of the interim agreement pending final agreement on the protocol agreement.

It also concluded that the November Terms were not superseded by the ongoing negotiations and exchanges of further terms and conditions in January and March 2002:

- "It would not make commercial sense that, while work was ongoing and the final contract was being negotiated, every new version of the terms and conditions sent between the parties would automatically supersede the original November Terms being worked under, unless the parties explicitly stated the same."

Perhaps the Court of Appeal was more inclined to overlook the non-specific nature of the November Terms and Arcadis' failure to expressly or formally accept the terms of the protocol in order to avoid the injustice of unlimited liability in circumstances when Amec was well aware of the existence of the proposed cap.

Harshness of the "extraordinary result"

Indeed, citing British Steel Corp v Cleveland Bridge & Engineering Co Ltd yet again, Gloster LJ referred to the harshness of the result of Coulson J's decision as another reason why he should have reached a different conclusion:

- "...if parties are in a stage of negotiation and one party asks the other to begin work 'pending' the parties entering into a formal contract, it cannot be inferred from the other party acting on that request that he is assuming any responsibility for his performance, except such responsibility as will be assumed under the terms of the contract that both parties are confident will be shortly finalised."

It would, therefore, be difficult to infer that Arcadis' liability was unlimited and that it was agreeing to accept more liability than it would have under the formal contract once finalised. The Court of Appeal's decision demonstrates that where a party accepts an offer by conduct, and is otherwise silent – such as here, where Arcadis did not reject any of the terms or make a counter-offer – it may follow that it has accepted all of the terms of the offer.

Practical lessons

In an ideal world, construction works should not commence until a final agreement is entered into. This is not always practical or possible. When *engaging a contractor under a letter of intent*, employers are encouraged to formalise the contractor's express agreement to the terms and scope of its instructions by counter-signature, and by doing so, entering into an initial binding contract. Parties should not be distracted by the parallel ongoing negotiations in reaching a final agreement of the building contract. Certain key issues, such as caps on liability, often driven by the terms of available insurance cover and with limited room for movement, should be specified and agreed. Terms and conditions of the agreement should not only be drafted with care, but should also be communicated (in other words, offered and accepted) with certainty.

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