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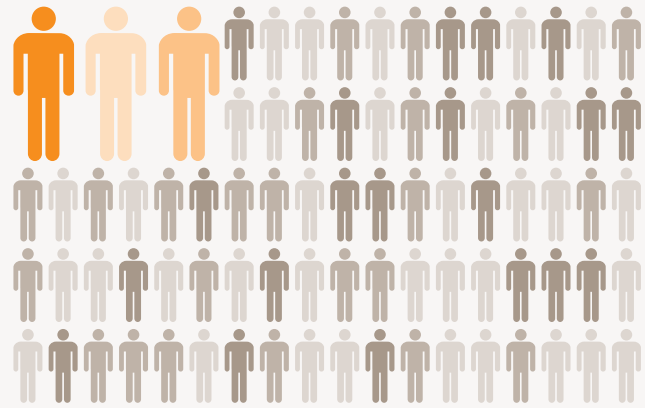
Law . Tax

Commercial Contracts Round-Up

September 2016

About CMS

32 new partners in 2015, taking the total to over 850



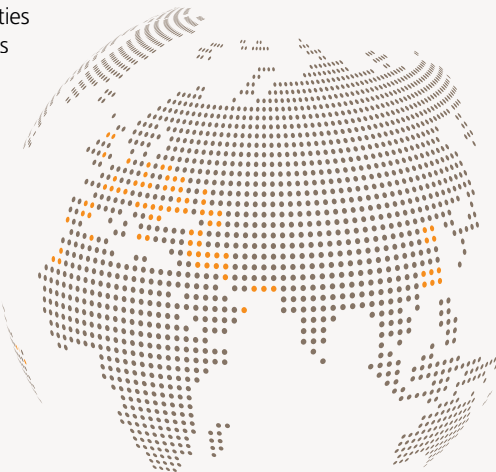
Top rankings
in 2015 M&A
League Tables
(by deal count)

#1 Europe
(Bloomberg,
Thomson Reuters)

#2 in Europe
(Mergermarket)

#3 Global
(Bloomberg
up to USD 500m)

Operating in 55 cities
across 35 countries



> 5,800 staff

> 3,200 lawyers

> 850 partners

EUR 1.01bn
turnover for 2015

19 practice
and sector
groups working
across offices

Ranked
2nd
most global
law firm
in the Am Law 2015
Global Top 100

Programme

Registration and breakfast 08.30
Welcome 08.55

Session One 09.00

Does your agreement mean what you think it means?
How are the courts approaching interpretation?

Drafting enforceable penalty clauses
E-contracts

Tea and coffee 09.55

Session Two 10.05

Brexit: contractual implications
Contract war stories: a litigator's perspective

Close 11.00

We would be delighted to discuss any of today's topics or related issues with you. You can find the contact details for all our speakers in the 'Contact the Speakers' section of this document.

Does your agreement mean what you think it means?

Kimberley Cross

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Interpretation of contracts – still developing! (1)

What's changed?

- Interpretation of contracts in a manner consistent with common sense
- The natural and ordinary meaning of words are key

Arnold v Britton & Others [2015] UKSC 36

- *“To pay to the Lessor without any deduction... a proportionate part of the expenses... in the repair maintenance renewal and the provision of services... the yearly sum of Ninety Pounds and value added tax (if any) for the first year of the term, increasing thereafter by Ten Pounds per Hundred for every subsequent year or part thereof.”*
- **“As Tolstoy said of unhappy families, every ill-drafted contract is ill-drafted in its own way.”**
- It is not the court's function to relieve a party from the consequences of imprudence or poor advice

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Recent Developments

- Literal interpretation
- Implied terms
- Variation in the face of anti-variation and express requirements
- Interpretation of exclusion of liability



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Interpretation of contracts – still developing! (2)

Since Arnold...

- *Canary Wharf v Deutsche Trustee Company Limited and others [2016] EWHC 100*
 - The words were **“clear and unambiguous”** (even though this meant an uncommercial result for one party)
- *Narandas-Girdhar & anor v Bradstock [2016] EWCA Civ 88*
 - Deleted words from previous drafts may be taken into account to resolve an ambiguity in the words

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Interpretation of contracts – still developing! (3)

- Lessons for the drafter
 - Trend is for courts to be more conservative; less willing to use common sense to interpret clauses
 - This means clear drafting is critical
 - Bear in mind the natural and ordinary meaning of the terms
 - Where language is clear, the courts will not step in to save a party from a bad bargain
 - Record the commercial background to a deal
 - Make sure the interpretation clause is fit for purpose
 - The more uncertain or ambiguous a clause, the more likely a court will use interpretation tools

Variation I: oral variation

What's new?

Oral variation is possible EVEN if you have a written clause purporting to prevent it

- Recent guidance provided in:
 - **Globe Motors Inc v TRW Lucas Varity Electric Steering Limited & Anor [2016] EWCA Civ 396:**
"... the fact that the parties' contract contains [an anti-oral variation] clause ... does not prevent them from later making a new contract varying the contract by an oral agreement or by conduct."
 - **MWB Business Exchange Centres Ltd v Rock Advertising Limited [2016] EWCA Civ 553:** "The clause which forbids a change, may be changed like any other. The prohibition of oral waiver, may itself be waived..."

Implied terms – filling the gaps

What's changed?

Marks & Spencer plc v BNP Paribas SSTC and another [2015] UKSC 72

A Court should only intervene to imply a term where:

- **business efficacy test:** it is necessary to give business efficacy to the contract; or
- **officious bystander test:** the term is so obvious that it goes without saying

Even then the Court should proceed with restraint

Avoid gaps through clear drafting!



Variation II: effect of express requirement for signature

What's changed?

A draft agreement can have contractual force even though an express requirement for a signature is unfulfilled

Reville Independent LLC v Aotech International (UK) Ltd [2016] EWCA Civ 443

"This Merchandising Deal Memo shall not be binding on Reville until executed by both Aotech and Reville".

A requirement for signature alone will not necessarily provide protection – parties should not assume the protection is there where work under a contract commences

Variation: lessons learned

- Establish procedures to define contracting authority and process
- Ensure your people (particularly contract managers) are aware that oral variation and variation by conduct is possible – verbal communications should be couched to ensure that contractual amendment is only possible in writing i.e. reserve your position!
- Conduct is key and no work should commence until the contract is settled
- Do still include oral anti-variation clauses in contracts, it will promote certainty through practice and evidence (but may not ensure it)



Conclusions

- The “natural” meaning of words in contracts are key, unless there is an ambiguity
- Ambiguity carries uncertainty both for the relevant clause and because it allows the court to interpret other aspects of the contract (including background arrangements)
- Conduct as well as written words can lead to ambiguity. Contracting procedure should be clear, although it may on occasion be appropriate to seek legal advice on conduct
- Full consideration of the circumstances of a contract and clear drafting of contracts are key to legal certainty



Exclusion of liability - loss of use, profit and production

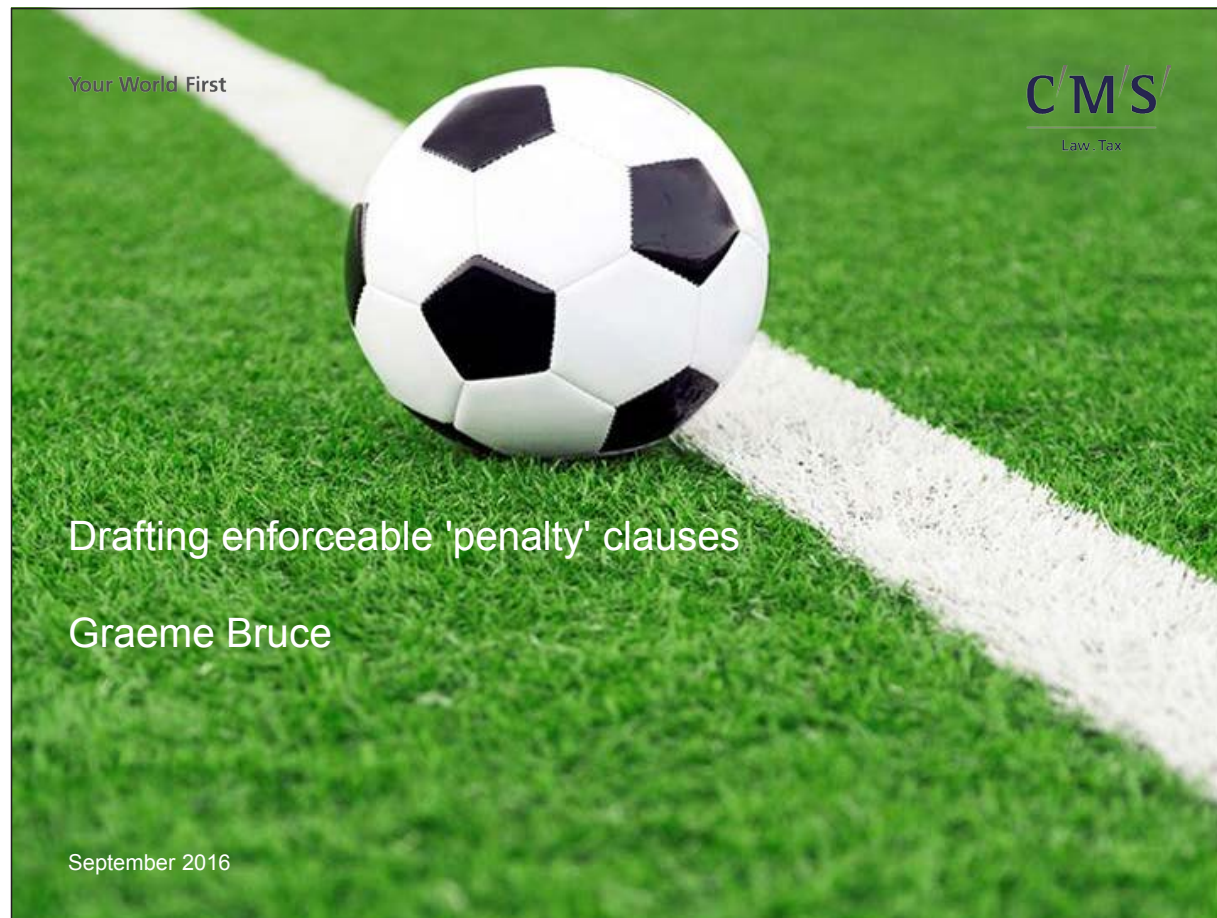
What's new?

Unless clearly drafted, exclusion clauses may be narrowly construed

Scottish Power UK Plc v BP Exploration Operation Company Ltd [2015] EWHC 2658

- “... **neither Party shall be liable to the other Party for any loss of use, profits, contracts, production or revenue or for business interruption howsoever caused and even where the same is caused by the negligence or breach of duty of the other Party.**”
- Losses identified by the High Court:
 - normal
 - secondary
 - indirect/consequential

The contract was seen to apply to secondary losses not “normal” losses



What is the penalty rule?

- Classic pre-Makdessi formulation:
 - “genuine pre-estimate of loss” – a contractual provision requiring the defaulter to pay money/forfeit an interest on default is unlawful **unless** it can be justified as a genuine pre-estimate of loss suffered by the innocent party on the breach
- Re-formulated following Makdessi

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Introduction

Cavendish Square Holding BV v Talal El Makdessi
ParkingEye Limited v Beavis – conjoined Supreme Court case -
Implications for the law of penalties in English and Scottish contracts

Lord Hodge:

“This issue affects Scots law as well as English law as the rule is essentially the same in each jurisdiction.....”

Maximising the chances of your drafting being enforceable

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What could be a penalty?

- Obvious example – payment of money –
 - on breach, party in breach must pay specified sum to innocent party
- Other examples potential ‘penalty’ provisions:
 - entitlement for innocent party to withhold monies otherwise payable to defaulter
 - forfeiture by defaulter of a deposit or other sum on default
 - obligation to transfer assets on default (perhaps for nothing/at undervalue)
 - any provision involving the forfeiture or diminution of defaulter’s rights on default



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What could be a penalty? Commercial context

- Trading contracts – lots of examples - payment of money on breach
- Corporate transactions
 - purchase agreements – withholding of deferred consideration; loss of options/other rights etc.
 - articles of association – disenfranchisement; forced transfer provisions; bad/early leaver penalties limiting sale price of shares etc.
- Energy/joint operating agreements/construction/joint ventures – forfeiture regimes
 - loss/diminution of rights
 - right of other party(ies) to acquire defaulter’s interests – sometimes uncompensated forfeiture

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The Cavendish/ParkingEye cases - general

- Good news for drafting contracts?
 - ***“In a negotiated contract between properly advised parties of comparable bargaining power, the strong initial presumption must be that the parties themselves are the best judges of what is legitimate in a provision dealing with the consequences of breach”***
 - Judicial recognition that not all adverse consequences of breach can be compensated by payment of money – sometimes need incentives to compliance – even if they look ‘penal’
 - Cavendish – facts
 - ParkingEye - facts

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What could be a penalty?

- Does there have to be a breach of contract before the rule is engaged?
 - Australia – recent developments - no
 - UK – Supreme Court - looked at and rejected Australian approach – YES

In the UK the penalty rule only regulates remedies available for breach of a party’s primary obligations – it does not regulate the obligations themselves



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Cavendish/ParkingEye – the new test

- New question/test:
 - **Is the clause penal?** (not ‘is it a genuine pre-estimate of loss?’)
 - Penal means the clause imposes :
 - ***“a detriment on the contract breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation”***
 - or, as Lord Hodge put it:
 - ***“the remedy is exorbitant or unconscionable when regard is had to the innocent party’s interests in the performance of the contract”***

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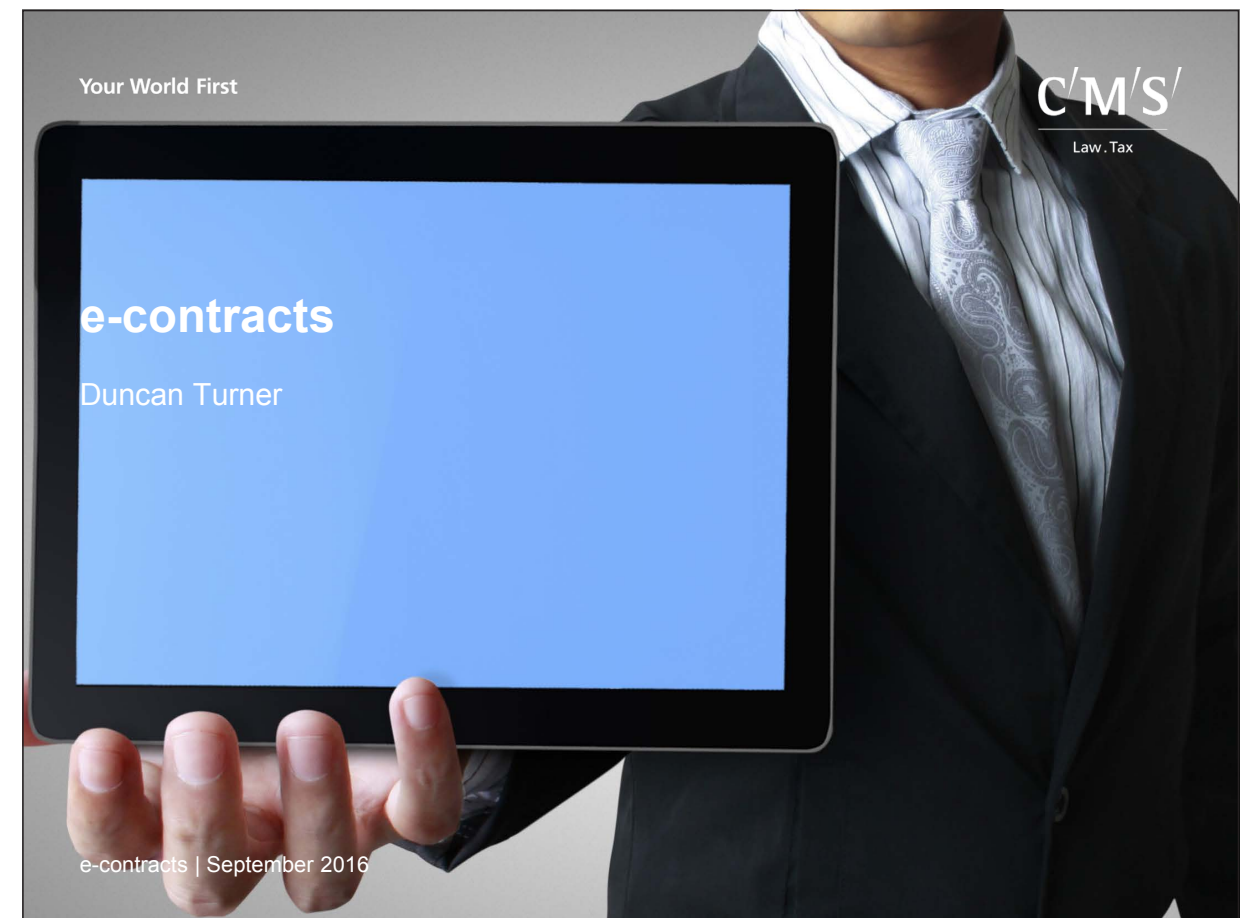
Round-up

Case should be good news but:

- application in particular circumstances (e.g. bad leaver in non share purchase scenario or uncompensated forfeiture) remains to be seen
- Scottish Law Commission currently looking at reform of Scots law on penalties

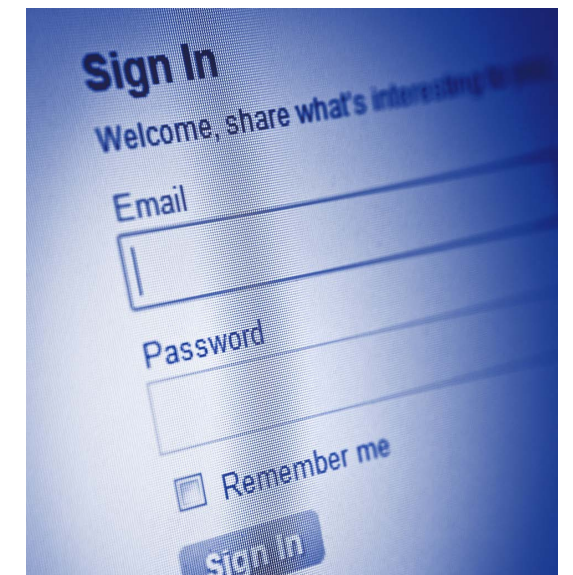
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Outline

- What is an e-contract?
- What are the requirements for forming a contract?
- Incorporation of terms
- E-signatures
- Forming contracts through exchange of e-mails



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What is an e-contract?

- Formation of a contract using electronic means
- Commonplace
 - website e-commerce
 - app-based trading
 - email exchanges
- Used increasingly for more formal contracts (which usually have more stringent requirements)



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Incorporation of terms

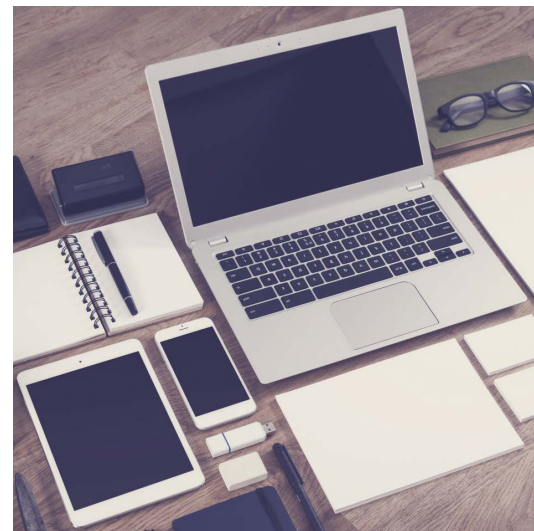
- Essential to ensure terms and conditions are incorporated into e-contract:
 - Have terms been clearly brought to attention of other party?
 - Is there evidence that other party acknowledged or agreed to terms?
- Limited case law on incorporation of terms in e-contracts
- Information requirements in e-contracts to ensure compliance with:
 - Electronic Commerce (EC Directive) Regulations 2002
 - Company, Limited Liability Partnership and Business (Names and Trading Disclosures) Regulations 2015
 - The Consumer Contracts (Information, Cancellation and Additional Charges) Regulations 2013 - consumers only

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What are the requirements for forming an e-contract?

- General rule: no writing or other form necessary to create legally binding contract
- However statutes impose particular formalities for some contracts (e.g. sale of land)
- The same principles apply to e-contracts



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e-signatures

- s 7(2) Electronic Communications Act 2000 (**ECA**):
 - anything in electronic form incorporated into or logically associated with an electronic communication or electronic data, which purports to be used for the purposes of establishing the authenticity or integrity of the communication or data
- For example
 - typing signatory's name into an email
 - scanning a manuscript signature, or
 - a digital signature
- ECA deems e-signatures admissible in court to evidence authenticity or integrity of an e-contract

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e-signatures: England & Wales

- Not clear that an e-signature will always satisfy requirement for contract to be “in writing” or “signed” - this will depend on statutory interpretation in each case
- Examples concerning the provision of guarantees:
 - *J Pereira Fernandes SA v Mehta*: inclusion of sender's name in email address was not sufficient to be “signed” in terms of s4 of the Statute of Frauds
 - *WS Tankship II v Kwangju Bank*: company name in the header of a SWIFT electronic message was sufficient to be a signature, as it had been “voluntarily affixed”
 - *Golden Ocean Group v Salgaocar Mining Industries PVT Ltd*: the typing of the sender's first name at the bottom of an email was sufficient to constitute a signature.
- **There is still some doubt that e-signatures can be used for executing deeds under English law**
- An e-signature may carry less evidential weight than an traditional wet ink signature in court proceedings

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Emails and binding contracts

Mi-Space (UK) Ltd v Bridgwater Civil Engineering Ltd [2015]

- Parties in dispute over payment due by Mi-Space to BCE
- Parties exchanged emails in attempts to settle dispute
- Mi-Space sent email offering to settle and asked BCE to confirm agreement. BCE responded that it was in agreement with proposal and asked Mi-Space to “carry on formalising the paperwork”
- Mi-Space sent formal Deed of Variation containing terms of settlement; BCE refused to sign



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e-signatures: Scotland

- The Requirements of Writing (Scotland) Act 1995 / Electronic Documents (Scotland) Regulations 2014
- An “advanced electronic signature” can be used for those contracts which must be “in writing” (other than wills and testamentary writings)
 - **This is an e-signature uniquely linked to the signatory, capable of identifying him/her, and is linked to the data to which it relates in manner that any subsequent change is detectable**
- Even where contract need not be in writing, an advanced electronic signature will carry greater evidential weight than a simple e-signature. Note however the requirement for e-signature to be certified by a third party if it is to be probative
- The Legal Writings (Counterparts and Delivery) (Scotland) Act 2015 permits documents signed on paper to be delivered electronically

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Decision

Court decided that parties had formed binding settlement in writing:

- Mi-Space's offer covered all matters in dispute and was clearly expressed
- BCE was unequivocal in its response and the acceptance was sufficiently formal to meet the requirements of the offer made by Mi-Space
- No sensible businessman could have thought that the other was intending anything other than the achievement of a legally binding agreement

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Lessons

- Settlement agreements, like other contracts, can be created by informal communications such as e-mail correspondence
- Important to make clear in e-mails that discussions are subject to contract



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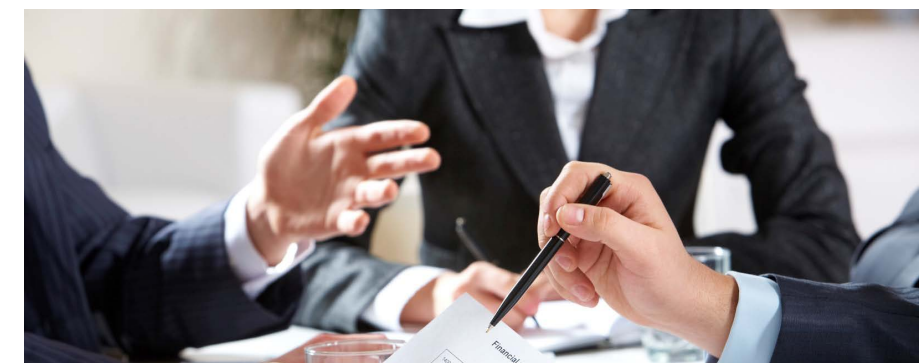
Brexit: Contracts and Cross-border Disputes

Graeme Macleod
Kushal Gandhi

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Overview

- Implications for contracting parties
- What does it mean for cross-border disputes?



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Implications for contracting parties

- Contractual interpretation: giving effect to the objective intention of the parties
- The court will not “*favour a construction which fits the likely purpose, influenced by knowledge of what has happened after the event, and forgetting other factors that may have influenced the parties at the time*” as to do so would be to “*seek to mend or improve the bargain that was actually made. The agreement must be construed as it was, not as subsequent events might suggest would have been wise to have made it.*”

Bank St Petersburg v Saveljev [2013] EWHC 3529 Ch [73]

Contracts: What To Do Next

- Existing contracts: review contracts or clauses which may be affected by BREXIT
- Future contracts: be aware of the range of contractual protections that may be sought



Implications for contracting parties

- BREXIT clauses
- *Force Majeure* clauses
- Material Adverse Change clauses
- Hardship
- Future legislation provision
- The doctrine of frustration



Cross-border Disputes: Jurisdiction

- Current
 - Recast Brussels Regulation
- Post-BREXIT
 - 2007 Lugano Convention
 - Hague Convention on Choice of Court Agreements
 - Bilateral / multilateral treaties



Cross-border Disputes: Recognition and Enforcement of Judgments

- Current
 - Recast Brussels Regulation
- Post-BREXIT
 - 2007 Lugano Convention
 - Hague Convention on Choice of Court Agreements
 - Bilateral / multilateral treaties



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Cross-border Disputes: Arbitration Proceedings

- New York Convention on Recognition and Enforcement of Foreign Arbitral Awards



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Cross-border Disputes: Governing Law

- Current
 - Rome I and Rome II Regulations
- Post-BREXIT
 - Rome I and Rome II Regulations
 - Contracts (Applicable Law) Act 1990



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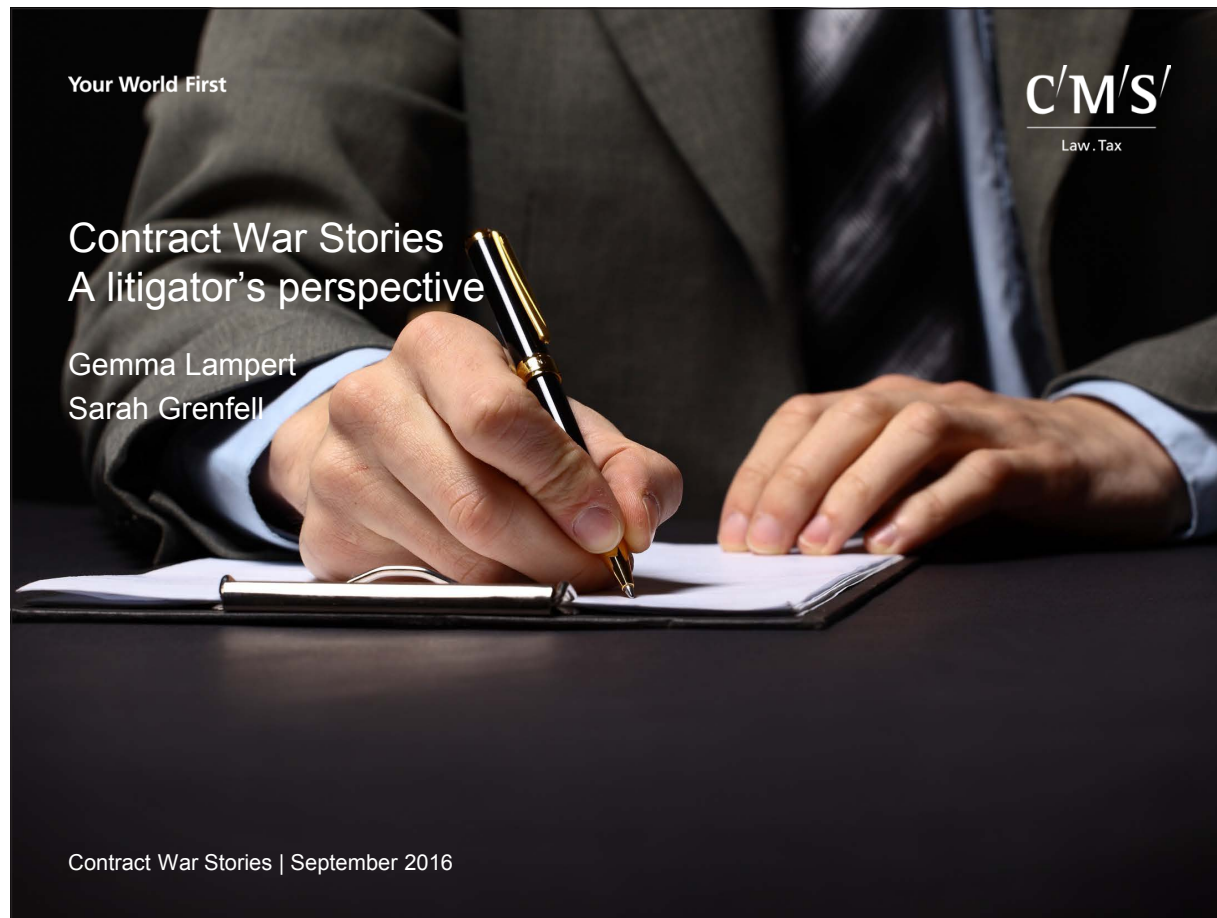
Cross-border Disputes: What To Do Next

- Enforce existing judgments without delay
- New contracts: arbitration agreement for dispute resolution?



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Why is a battle plan needed?

A few practical steps along the way could prevent much grief

We spend every day resolving contract breakdown

Litigation is a significant industry worldwide

Cost, time and trouble for business should not be underestimated

When things go wrong losses often outweigh profits

Even the winners rarely appreciate the process

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Agenda

Why is a battle plan required?

When are the casualties suffered?

Achieving victories

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When are your troops vulnerable?

Pre Contract

Changing the Contract

Termination

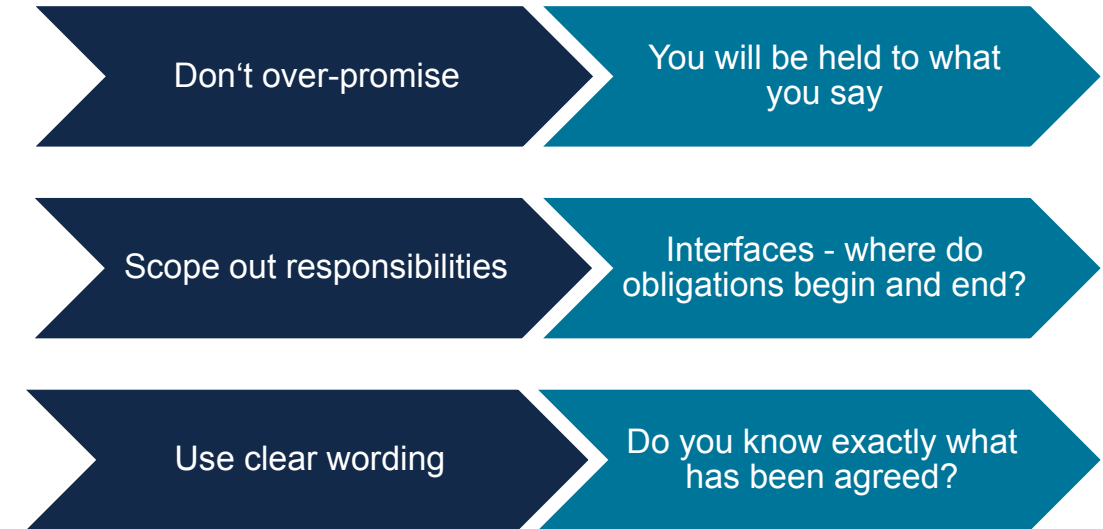
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War Stories – Pre Contract



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Securing the high ground



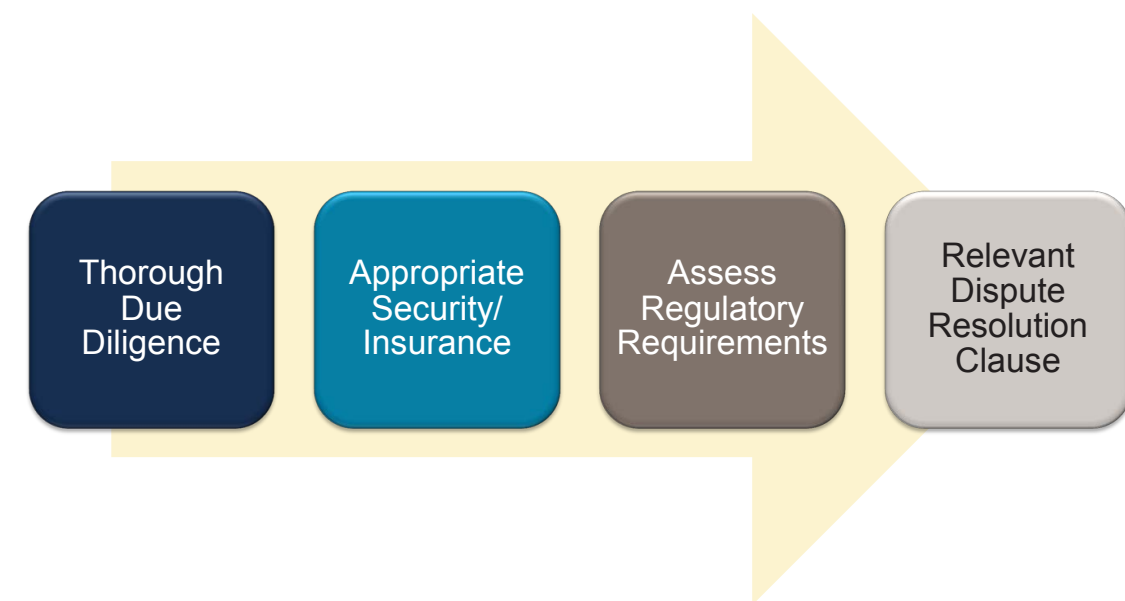
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Pre – Contract: Getting your troops in the right position is key



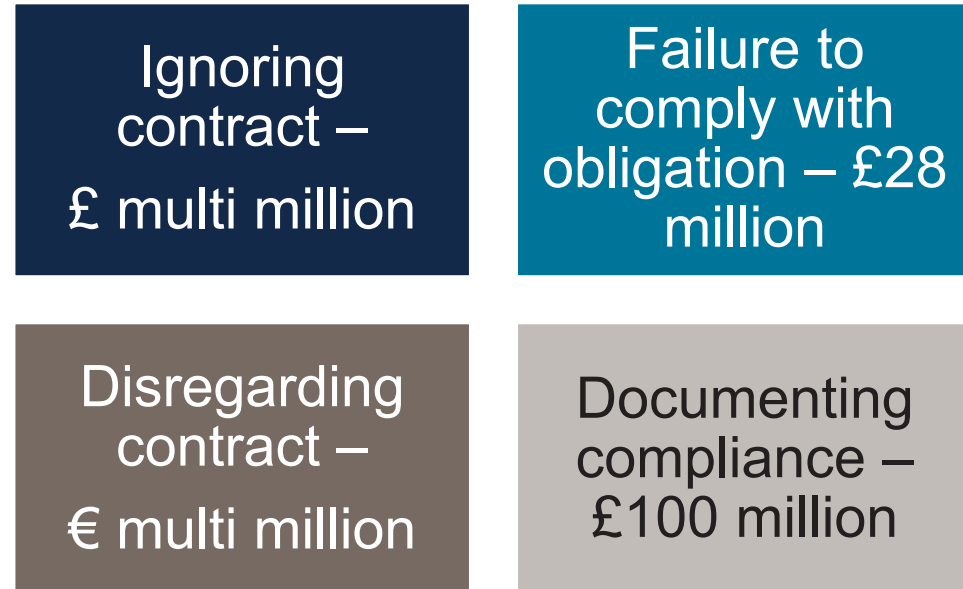
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Get your battle support in place



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War Stories – During Contract



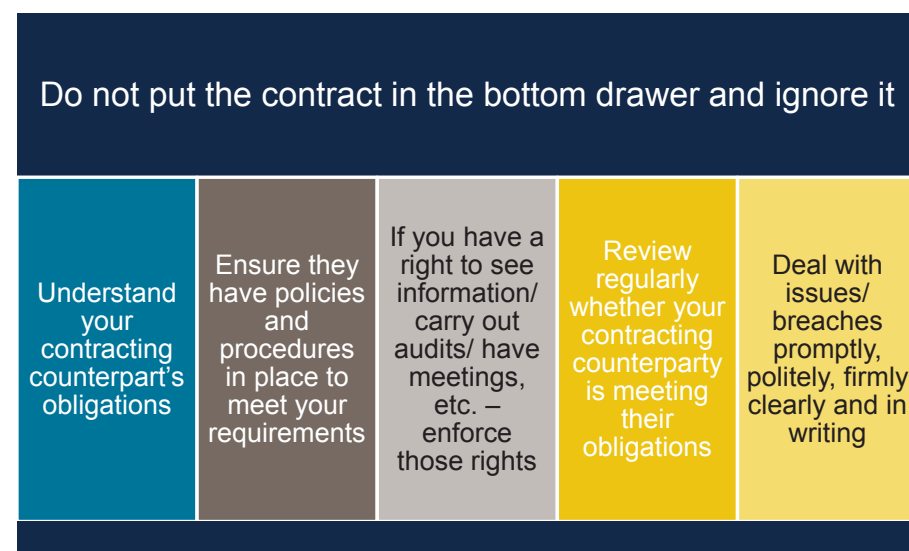
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Be wary of violating borders



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During the Contract: Understand how to use your weapons



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Respond to changing conditions?



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War Stories – Termination

Inaccurate drafting of notices – €7 million

Consider quantum – €7 million

Failure to document issues clearly – \$4 million

Consider handover before terminating – £3 million

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Termination – Facing the cannons

Understand the consequences of termination before terminating

If you have suffered losses are there limitations/exemptions capping your recovery

Consider the need for services to continue – manage transfer to a new provider

Wrongful termination is a breach of contract – you may face/be able to bring a claim for considerable damages

Do the facts support termination and show the breach is sufficiently serious to justify termination?

Document problems in the lead up to termination – to provide supportive evidence or to oppose termination

Act professionally during the termination process

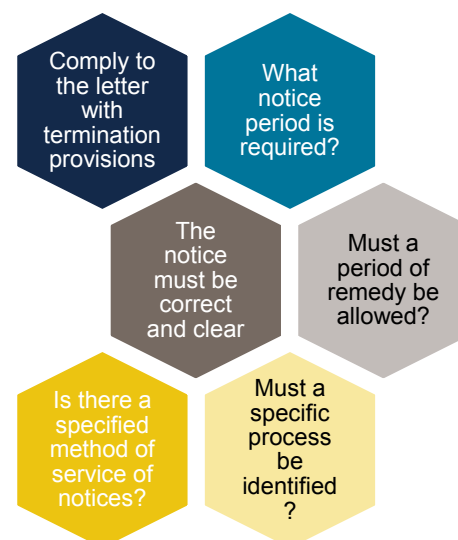
React to notices and respond clearly and promptly in writing if termination is opposed

Act promptly if relying on a breach, or you may be treated to have accepted it

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Notices: Adhere to the rules of engagement

“If the clause had said that the notice had to be on blue paper, it would be no good serving a notice on pink paper, however clear it might have been that the tenant wanted to terminate the lease.”



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Conclusion: Winning the battle



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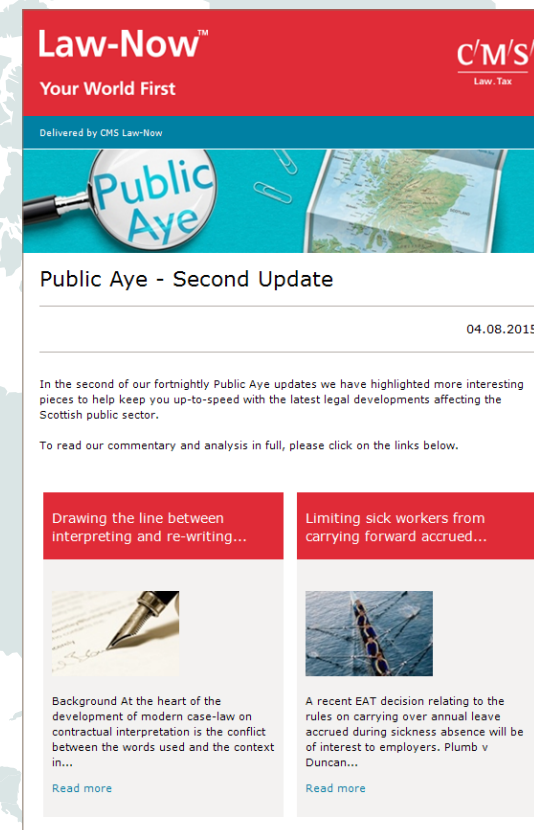
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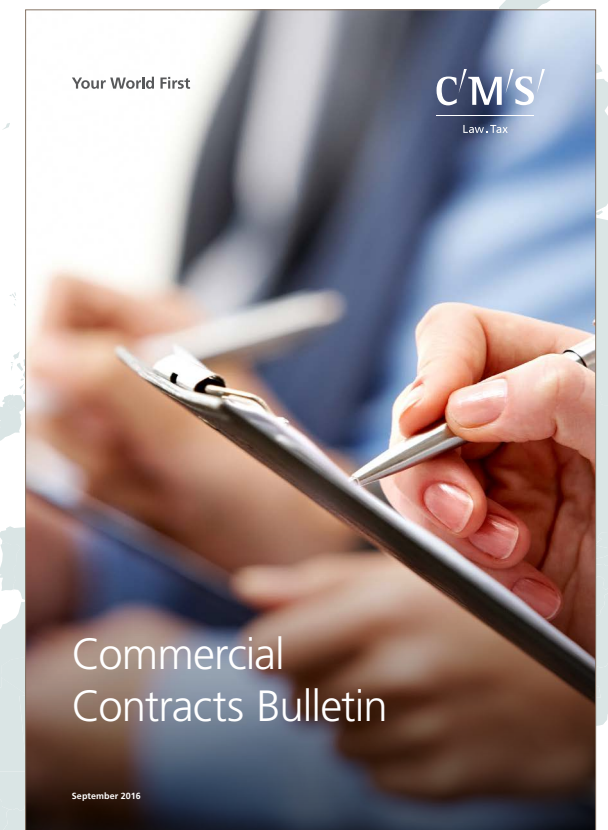
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