



Technical

## Contract Formation and Interpretation

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### Another Brick in the Wall

1. Sometimes we tend to think that construction law is somehow ring fenced from the general law. This is, of course, not the case and most of the fundamental principles which we use in construction contracts are derived from cases which fall outside of the construction industry.
2. In December 2010 the case of *Pink Floyd Music Limited -and- EMI Records Limited [2010] EWCA Civ 1429* was heard in the Court of Appeal. The case involved the interpretation of the terms of a contract between the Pink Floyd and EMI which was entered into in June 1999. The principles involved are the same as we see in many construction contracts where the terms are ambiguous. Of course, EMI chose to interpret the terms to its benefit resulting in a dispute over many millions. There were two main issues on which the Court of Appeal was asked to decide. These were:
  - the basis of the calculation for Pink Floyd's percentage of royalties; and
  - the selling of single tracks rather than albums in digital form e.g. iTunes.

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## Grab that Cash with Both Hands and make a Stash

3. The approach taken by the Court of Appeal to contract interpretation in this case is the same as would apply in a construction case. Lord Neuberger referred to cases such as *Investors Compensation Scheme Limited -v- West Bromwich Building Society* [1998] and *Chartbrook Limited -v- Persimmon Homes Limited* [2009] both judgments of the House of Lords. He said:

*“Each of the declarations... raises a question of interpretation of a provision in a commercial contract. The answer to such a question does not simply depend on the words used in that provision; it is also dependent on the other provisions of the contract, on commercial common sense and on the surrounding circumstances...”*

*The ultimate aim of interpreting such a provision is to determine what the parties to the contract meant by it. And... the words... cannot be interpreted in a vacuum...”*

4. Both sides argued that there was significant ambiguity and mistakes in the drafting.
5. On the first issue the argument about the percentage addition for receipts which were used as the basis for calculating royalties, EMI said that there was a mistake, whereas Pink Floyd said that EMI had not established

*“that the words actually used produced a result which is so commercially nonsensical that the parties could not have intended it.”*

6. The Court of Appeal decided that although it might be that the agreement did produce an unexpectedly favourable result for Pink Floyd it could have been that they were able to command a particularly favourable rate and agreed with Pink Floyd's interpretation of the contract.

## I'm Alright, Jack - Keep Your Hands off my Stack

7. The second issue, that is the selling of records as singles (e.g iTunes) without Pink Floyd's consent involves very similar issues. The contract was considered to be ambiguous and there were arguments about the interpretation of the word record. Did this, for example, include digital recordings. The contract included a number of defined terms but then the same terms were apparently used in a different context which created the uncertainty. On this issue Lord Neuberger decided on the wording of the contract and said that:

*"It is therefore quite permissible, indeed positively appropriate, to invoke commercial common sense to assist on the issue of the clarifying the rather opaque provision."*

8. It was decided, therefore, that he would interpret the contract using commercial common sense and again interpreted the contract in the way argued by Pink Floyd.

## A Momentary Lapse of Reason?

9. The decision of the Court of Appeal was a majority decision. Lord Carnwath the dissenting judge said:

*"The same principles leave me respectfully to differ... on the second issue. Important points to my mind are the prima facie assumption that the words mean what they say; the dangers of "detailed and semantic syntactical" analysis of a commercial document; and the warning against too readily inferring that something has gone wrong merely because it appears to result in a bad bargain..."*

10. Lord Carnwath agreed with Lord Neuberger on the first issue but did not think that the wording and use of the words records and albums was ambiguous and would have found in favour of EMI.

## Uncomfortably Numb

11. We are all aware that construction contracts often turn out to be ambiguous although at the time they are entered into we believe (or hope) that the contract reflects the deal we have made. This was obviously the case between Pink Floyd and EMI. The contracts had been specifically drafted and it was not until around ten years later that Pink Floyd's auditors spotted the problem with the way that EMI had been interpreting the agreement.
12. Often we are faced with a bundle of documents that contradict each other or are at best uncertain. Over the years a body of case law and other authorities have helped us interpret, for example the JCT or ICE suites of contracts. Even with that history and body of law behind us it is still often a difficult task to interpret the contracts.
13. Examples of this are *Fenice Investments Limited -v- Jerram Falkus Construction Limited* [2009] and *WW Gear Construction Limited -v- McGee Group Limited* [2010].
14. In Fenice the court decided that the claimant could rely on the priority of documents clause in a JCT contract, although this perhaps did not reflect the bargain the parties had entered into. In WW Gear, a dispute about the issuing of relevant notices and condition precedent machinery, the court adopted similar principles to *Pink Floyd -v- EMI* (he referred to *Investors and Chartbrook*) and interpreted the contract such that it made commercial sense despite some errors in the drafting.
15. There are many other examples in the construction industry where many of us will consider that the interpretation of the contract has followed the same sorts of principles as in Pink Floyd and EMI (and many other commercial cases).

## Us and Them

16. Nick Mason (Pink Floyd's drummer) told the BBC that he was "very fond" of EMI and that the court case was not "a big punch up" but rather about getting a third party to adjudicate. Perhaps in construction contracts it goes too far to say that the parties are very fond of each other but often disputes do end up in a big punch up or in adjudication.

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