A common cause of disputes in EPC Contracts can be conflicting or ambiguous wording in the contract.

The process of agreeing the terms of an EPC contract can often be carried out under significant time pressure. Whether the Contract is bespoke or there are extensive amendments to a standard form contract such as FIDIC, there is a risk that the insertion of new provisions can make the contract appear ambiguous in places. These uncertainties can be seized upon by parties where they can give rise to potential entitlement to change and thereby additional time/money. For major infrastructure projects, there can also be extensive schedules to the contract which may also contain conflicting or ambiguous provisions.

In that context, we look at key principles in English law that will assist when disputes over contract interpretation arise. These points highlight the key issues and general rules which need to be considered – based upon a large body of English case law on this issue.

Precedence

1. Order of Precedence

A good starting point when an ambiguous or conflicting provision exists within a contract is to check the order of precedence typically set out within the document. This order of precedence will rank documents of the contract such that it should be clear which documents take precedence.

This mechanism will often rank bespoke amendments over standard form provisions, but will need checking in each instance.

More significant problems can arise where there are conflicts between provision within the same contract document or where contract documents are equally ranked.
2. The whole contract needs to be considered

First, a very old rule (which remains good law) is that you look at the contract as a whole to understand its overall commercial purpose. Lord Halsbury, in Glynn v Margetson [1893] A.C. 351, said:

“Looking at the whole of the instrument and seeing what one must regard...as its main purpose, one must reject words, indeed whole provisions, if they are inconsistent with what one assumes to be the main purpose of the contract.”

It is a serious error to interpret contract clauses in isolation. The context of the whole contractual agreement between the parties is key. Only a full understanding of the whole agreement will provide clarity as to each party’s intentions when they entered into the contract.

3. Contract interpretation is not an exact science

The rules of contract interpretation have developed organically. Modern case law suggests that there is no strictly defined approach. Most principles of contract interpretation are broadly regarded as guidelines. These guidelines are however closely considered should a tribunal or court be asked to provide its view as to how a contract should be interpreted.

In recent years, the general trend has seen a movement away from an overly literal approach to contract interpretation towards what has become known as the “purposive” approach.

4. Look closely at the words themselves

The starting point for analysis is the use of language in the contract. The case of Pink Floyd Music Limited v EMI Records Limited [2010] EWCA Civ 1429 reaffirmed that there exists a prima facie assumption that ordinary English words will mean what they say. This means if the words of the contract are clear and unambiguous then it should be assumed that the provisions of the contract are those that the parties meant to include.

When interpreting a contract the “ordinary” meaning of words should be applied in the first instance. When the facts of the case are applied to an interpretation of the “ordinary” meaning of the words in the contract and an unambiguous or straightforward result is achieved, it is unlikely that further interpretation will be needed.

5. An objective test should be applied

However, in cases of uncertainty, it is rarely the case that the words in a contract are clear and unambiguous when given even their “ordinary” meaning. As a result, the courts have needed to review how best to examine contract interpretation.

To provide clarity as to how contract interpretation beyond the “ordinary” meaning of words should be defined, Lord Hoffman in Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 W.L.R. 896, 912 set out that an objective test should be applied.

Lord Hoffman was clear that the objective test meant more than just looking at the words in the contract in their ordinary meaning. He said, “the meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean.”

In short Lord Hoffman’s test asked ‘what would a reasonable man interpret to be the meaning of the contract?’
6. The objective test is wider than just the words in the contract

In the Court of Appeal case of NLA Group Ltd v Bowers [1999] 1 Lloyds’ Rep 109, the Court confirmed Lord Hoffman’s view that it is necessary to look at “all the relevant background information where there is a confusing clause or a mistake in a clause which needs resolving.”

It is too vague however to say that “all relevant background information” needs to be considered when seeking to interpret a contract. In a construction and engineering project for example this could include tender negotiations, contemporaneous correspondence dating from the time the contract was agreed and even circumstances after the date the contract was formed. Such a scope is clearly too wide and examination of every piece of potentially relevant background information would be inefficient and costly.

The relevant context for the purposes of contract interpretation has therefore been further defined.

7. The circumstances surrounding the formation of the contract are important

Lord Hoffman went on to describe the relevant contextual information as “all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract … it includes … anything which would have affected the way the language of the document would have been understood by the reasonable man”.

Although clearer, this remains a wide context. Anything which could have influenced either party’s intention when it entered into the contract may in fact be an important piece of evidence should a question of contract interpretation arise. A communication which seems unimportant when a contract is formed may in fact prove to be crucial when seeking to analyse the intention of the contracting parties when the contract was signed. Document management on projects even at a pre-contract stage is therefore key.

8. What happens after a contract is formed is irrelevant

When interpreting a contract the key issue is what the parties’ understanding and intention ought to have been at the time the contract was made.

The recent Technology and Construction Court case of MT Højgaard v E.ON Climate and Renewables UK Robin Rigg East Limited [2014] EWHC 2369 confirmed that this principle remains a key part of contract interpretation.

The Court held that “The actual circumstances applicable … would involve post contract conduct, not usually an admissible guide to interpretation.”

Often when a dispute occurs, contracting parties can become preoccupied by events which post-date the agreement of the contract. These events are seen as irrelevant to what the contract properly means by courts and tribunals. Subsequent events may shed some light on the contract’s interpretation but cannot change the fundamental meaning.

Although it seems harsh, this position is understandable. If post conduct events were taken into account the result might flow that a contract means one thing the day it is signed but, by reason of the subsequent event, means something different the day after.
9. The commercial purpose of the contract is key

It is possible, and sometimes appropriate, to add a commercial, common sense angle to contract interpretation.

In fact, if the words in a contract would impose upon a party a responsibility which is clearly not in line with commercial reality then it may be sensible to depart from consideration of the ordinary and plain meaning of words. Lord Diplock in the House of Lords confirmed this in the case of Antais Compania Naviera SA v Salen Rederierna AB [1985] AC191 by saying:

“if detailed semantic and syntactical analysis of a word in a commercial contract is going to lead to a conclusion that flouts business common sense, it must be made to yield to business common sense”.

This will only go so far – a contract cannot be re-written just to reach a business-like result. However, if there is more than one interpretation then the court or tribunal will likely give effect to what can be seen as the commercial purpose of the agreement.

10. “Business common sense” is itself a wide concept

The “business common sense” principle was reinforced in the recent TCC case of The Trustees of the Marc Gilbard 2009 Settlement Trust v OD Development and Projects Limited [2015] EWHC 70. A dispute arose under between the parties with regard to the validity and correctness of a Final Certificate on a construction project. The contract stated that disputes regarding payment certificates had to be brought within a 28 day period. One of the parties tried to bring more than one dispute, outside of the 28 day period.

In interpreting the contract, the court applied business common sense. It was, in the court’s view, clear that the parties intended to cap their commercial exposure to the legal costs of dispute resolution by imposing a strict time limit on when dispute proceedings could be brought. Any attempt to bring further proceedings after the 28 days was contrary to business common sense and therefore contrary to the intention of the parties.

“Business common sense” does not just include direct commercial concerns e.g. profits or project costs, but can also extend to legal costs of disputes that may never have been anticipated at the date the contract was agreed.

Disputes on the correct interpretation of EPC contracts are always going to be difficult to resolve – EPC Contracts are complex and can be lengthy. Projects are high value and are also complex.

When a dispute over what a Contract means arises, there are no easy answers. Detailed analysis of the contract as a whole is required. In many circumstances, this is likely to resolve any inconsistency or ambiguity. However, where it does not, a more detailed review of contract documents and the intent of the parties will be required. Because these exercises can be so difficult (and therefore expensive), disputes over points of interpretation should be avoided if at all possible. Where that is unavoidable, seeking legal advice should be a priority.