Out of gas

Doug Wass and Nikolas Ireland provide an update on contractual remedies

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'While the principle remains that a party does not intend to give up common law rights without making it clear it intends to do so, it should not operate as a blind presumption to the detriment of proper analysis of the clause in question.'

The Court of Appeal's recent decision in *Scottish Power UK plc v BP Exploration Operating Company Ltd* [2016] has given guidance on the approach the court should take when considering whether a contractual remedy for a breach of contract should be interpreted as the sole remedy for that breach to the exclusion of all other common law remedies.

At a glance

Lord Diplock stated in the House of Lords case of *Gilbert-Ash (Northern) Ltd v Modern Engineering (Bristol) Ltd* [1973] that when considering a contract excluding legal rights or remedies:

> ... one starts with the presumption that neither party intends to abandon any remedies for its breach arising by operation of law, and clear express words must be used in order to rebut that presumption.

In the absence of clear, express words it has proved very difficult for parties seeking to demonstrate that legal rights have been excluded to overcome such a presumption.

The case of *Scottish Power* has provided Court of Appeal authority that such a presumption should not be rigidly applied but, instead, the natural meaning of the words should be given effect even if that results in a party losing legal rights and remedies it would otherwise have had.

Case facts

The case concerned an oil and gas field off the coast of Scotland in the North Sea (the Andrew Field) owned by BP and others (the sellers). A dispute arose between the sellers and Scottish Power UK plc (the buyer), who was the buyer of gas pursuant to four nearly identical long-term gas sales agreements (the agreements).

Due to a shutdown of the Andrew Field for modification of the facilities to allow it to 'tie in' with a nearby oil and gas field, the sellers were unable to meet their obligations to supply gas under the agreements between May 2011 and December 2014.

Clause 16 in each agreement provided a mechanism whereby, if the seller failed to supply the agreed amount of gas, the seller was obliged to supply an equivalent amount of gas to the buyer at a discounted rate once production had restarted. This compensatory price was defined in the agreements as the 'default gas price'.

During the shutdown, the buyer sourced gas from alternative providers to meet its needs but the price of the replacement gas was higher than the contract price it would have paid under the agreements. The buyer sought to claim these losses from the sellers as damages for a breach of contract. The sellers accepted that they had breached the agreements but said that the buyer's remedies in relation to underdeliveries of gas were limited to the contractual remedy contained in clause 16 of the agreements.

While the buyer agreed that the sole remedy for an underdelivery of gas was the default gas price, it sought to claim that in failing to operate the facilities during the shutdown the sellers were also in breach of clause 7.1, which stated:

> Throughout the Contract Period the Seller will, in accordance with the Standard of a Reasonable and Prudent Operator, provide, install, repair, maintain and operate those Seller's

> Facilities which are (in the opinion of the Seller and the other Sellers) necessary to produce and deliver at the relevant times the quantities of Natural Gas from the Andrew Field which are required, in accordance with the terms of this Agreement, to be delivered to the Buyer at the Delivery Point.

for the alternative gas and the price of the gas under the agreement, after credit had been given for gas subsequently provided at the default gas price which, as mentioned above, applied in the event of an underdelivery.

The sellers said that the default gas price was intended to provide the sole remedy in respect of underdeliveries and that the damages claimed by the buyer were due to the underdelivery of gas. It said that despite the underdelivery having been caused by the shutdown, which in itself was a breach of clause 7.1, this did not prevent clause 16 from operating as the sole remedy. The sellers relied upon clause 16.6 which stated (emphasis added):

> The delivery of Natural Gas at the Default Gas Price and the payment of sums due in accordance with the provisions of Clause 16.4 shall be in full satisfaction and discharge of all rights, remedies and claims howsoever arising whether in contract or in tort or otherwise in law on the part of the Buyer against the Seller *in respect of underdeliveries* by the Seller under this Agreement, and save for the rights and remedies set out in Clauses 16.1 to 16.5 (inclusive) and any claims arising pursuant thereto, the Buyer shall have no right or remedy and shall not be entitled to make any claims in respect of any such underdelivery.

The buyer said that the default gas price was not intended to be the sole remedy for breaches of clause 7.1 and that it was therefore entitled to damages for breach of contract.

The buyer said that the default gas price was not intended to be the sole remedy for breaches of clause 7.1 and that it was therefore entitled to damages for breach of contract (which were said to amount to some £85m). These damages were quantified as being the difference between the amount it had to pay

The key question for the purpose of this article is how the court interpreted clause 16.6 and whether the default gas price was the exclusive remedy available to the buyer in relation to its claim for the breach of clause 7.1 of the agreements.

Commercial Court and Court of Appeal decisions

Leggatt J ruled that clause 16.6 was comprehensively drafted and, while the words 'in respect of underdeliveries' were not precise and could give rise to an alternative interpretation which resulted in the remedial regime applying in much narrower circumstances, this was not the correct interpretation.

The default gas price was an automatic remedy in the case of an underdelivery of gas as opposed to a remedy which could be nominated by the buyer as an alternative to a damages claim. As the default gas price was an automatic remedy, allowing the buyer an additional remedy for a failure to deliver the same quantity of gas would be an 'improbable intention' of clause 16.6. The words 'in respect of underdeliveries' brought the buyer's claim within the exclusion and it was stated by Leggatt J that:

> ... where a breach of [clause] 7.1 causes loss by way of an underdelivery for which the Buyer automatically receives compensation pursuant to [clause] 16 in the form of Default

> Gas, that remedy is in my opinion intended to be the sole remedy available for the loss.

This interpretation of clause 16.6 did not strain the ordinary meaning of the words and it was confirmed that where a breach of clause 7.1 did not result in an underdelivery, that loss would not be limited by the default gas price regime. The contractual remedy was the sole remedy where the loss was suffered due to an underdelivery, as was the case here.

While Leggatt J stated:

> I have not overlooked the presumption that parties do not intend to abandon remedies that arise by operation of law. It seems to me that this presumption must be less strong where the common law remedy is not simply excluded but is replaced by a different (and valuable) contractual one...

the buyer appealed the decision on the basis that the judge had lost sight of the principle outlined in *Gilbert-Ash* that there is a presumption that the parties do not intend to give up rights or claims which the general law gives them. It was argued that, as the judge held that there were two possible meanings of clause 16.6, he should have adopted the narrower meaning which did not involve the buyer giving up valuable rights.

The Court of Appeal upheld the decision of the Commercial Court and gave some important guidance as to how exclusion clauses should be interpreted. While the principle remains that a party does not intend to give up common law rights without making it clear it intends to do so, as set out in *Gilbert-Ash*, it should not operate as a blind presumption to the detriment of proper analysis of the clause in question. Clarke LJ stated that the fact that there are two possible meanings of clause 16.6 is simply the beginning of the interpretation exercise as opposed to the basis upon which the court must instantly interpret the clause in a way which results in a party's legal rights not being lost.

The court referred to the Court of Appeal decision in *Nobahar-Cookson v The Hut Group Ltd* [2016] which confirmed that the principle is not:

> ... simply to be mechanistically applied wherever an ambiguity is identified in an exclusion clause.

Instead, it is necessary for the court to apply:

> ... all its tools of linguistic, contextual, purposive and common sense analysis to discern what the clause really means.

If this exercise results in a clear answer then that must be given effect even where it deprives a party of legal rights.

As the default gas price was an automatic remedy, allowing the buyer an additional remedy for a failure to deliver the same quantity of gas would be an 'improbable intention' of clause 16.6.

A further important point to note from Clarke LJ's judgment is that the principle will be further weakened where the legal rights of a party are not simply being excluded but are being replaced with an alternative remedy. This therefore suggests that the court will be influenced in its interpretation of exclusive remedy clauses depending on the extent of the contractual remedy (if any) replacing it.

Conclusion

This judgment corroborates the general legal trend in interpretation of contracts and reflects cases such as *Arnold v Britton* [2015] which show the court treating the natural meaning of language as the best guide to interpretation. Indeed, it is difficult to interpret clause 16.6 in any other way when the natural meaning of 'in respect of underdeliveries' is considered, even in light of the resulting inability of the buyer to recover its losses.

The now often-cited mantra that the court will not intervene to save a party from a bad bargain could ring true in this case where the court clearly took the opinion that the sophisticated parties had chosen to provide for a contractual remedial scheme which would replace all other legal remedies in relation to underdeliveries. *Nobahar-Cookson* provides further grounding for this sentiment and recognises that:

> ... commercial parties are entitled to allocate between them the risks of something going wrong in their contractual relationship in any way they choose.

The simple fact that it transpired that the common law rights replaced in the present case were of far greater value to the buyer than the default gas price regime was not a reason to change the natural meaning of the words used by the draftsman.

Finally and most importantly, the case has changed the way in which the court may now approach cases where there is a dispute as to whether a contractual remedial regime was intended to provide the sole remedy for breach of contract to the exclusion of all other claims. In circumstances where an exclusion clause has alternative possible meanings, there is no longer a strict presumption which requires the court to choose the meaning which avoids a party being found to give up legal rights. Instead, the court will treat this fact as the beginning of the enquiry as opposed to its end and approach the exercise with a linguistic, contextual, purposive and common sense analysis, with a view to finding out what the clause really means, even if that results in a party losing valuable legal rights. ■

Arnold v Britton & ors
[2015] UKSC 36

Gilbert-Ash (Northern) Ltd v Modern Engineering (Bristol) Ltd
[1973] 3 WLR 421

Nobahar-Cookson & ors v The Hut Group Ltd
[2016] EWCA Civ 128

Scottish Power UK plc v BP Exploration Operating Company Ltd & ors
[2016] EWCA Civ 1043