INSIGHT

Credit: Nickbenagh, Creative Commons Attribution-Share Alike 3.0 (Wikipedia)

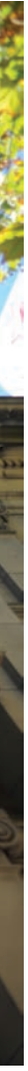
Supreme Court of Victoria, Melbourne

The work has been done, but was there a contract in place?

Andrew Laird
Melbourne TEC Chambers

A recent case from the Supreme Court of Victoria, Australia, provides an example of how the courts approach the inevitably complicated situation which arises where parties proceed with construction work without having executed a formal contract.

Time pressures on construction and engineering projects are relentless. Contractual negotiations sometimes continue even as the first sod needs to be turned. Normally contracts are formally executed at some point but sometimes they are not. Often a lack of formal execution evaporates as an issue because both parties acknowledge the existence of a contract. Sometimes, however, a party asserts that the relationship never reached contractual status, frequently as a precursor to a claim for a quantum meruit.



Credit: Nickbenanh, Creative Commons Attribution-Share Alike 3.0 (Wikipedia)

With this in mind, a recent Victorian Supreme Court decision in the matter of *Skilled Group Ltd v CSR Viridian Pty Ltd & Anor*[1] will be of interest to readers around the world. It considered the following important issues:

- when the existence of a contract can be inferred in the absence of a signed agreement; and
- whether a party can be estopped from denying the existence of a binding contract in a particular form where it is found that a contract does not exist.

What happened?

The second defendant (Pilkington) sold its Australian operations to the first defendant (CSR). As part of the sale agreement, Pilkington agreed to help CSR refurbish and repair an existing float glass manufacturing facility at Dandenong in Victoria. Under the contractual arrangement between CSR and Pilkington, subcontractors were to be retained by Pilkington who would then be reimbursed by CSR. This arrangement was subsequently varied for administrative convenience to allow CSR to pay Pilkington's subcontractors directly.

Pilkington let a number of works packages to various subcontractors, including three separate packages to the plaintiff (Skilled). It was intended that Pilkington and Skilled would enter into three separate subcontracts for the works packages awarded to Skilled. Skilled commenced initial works in March 2008, before subcontracts were finalised. As the Court noted, this is not unusual where the interests of a project demand that the parties get on with the works.

The subcontract terms proposed for the works packages awarded to Skilled (the 'Skilled packages') were based on the standard Form AS 2124-1992 as amended by negotiated special conditions. The final form of the special conditions was agreed in late April 2008 (the 'agreed terms'); however, Skilled and Pilkington were still negotiating milestone dates and dates for practical completion at that time. These dates were important because, under the agreed terms, the date for practical completion and a separate interim milestone were to be the triggers for the subcontract liquidated damages regime, and Skilled indicated that it was unwilling to formally execute subcontracts until those dates had been agreed.

Skilled continued to perform works through to approximately November 2008 without formal execution of subcontract documents and without having expressly agreed on dates with Pilkington for practical completion or the separate liquidated damages milestones. While there was a limited amount of correspondence chasing executed subcontract documents, this petered out and the contemporaneous focus during the project was largely on getting the job finished.

Notwithstanding the absence of formal execution and express agreement on dates for practical completion and the separate liquidated damages milestones, there was quite a bit of conduct that suggested that Skilled and Pilkington had entered into contractual relations. For example, a superintendent was appointed to whom Skilled made variation and extension of time claims and Pilkington made claims for back charges and liquidated damages. Skilled also provided Pilkington with bank guarantees as security.

The various Skilled and Pilkington claims were assessed by the superintendent, who ultimately issued final certificates for each of the Skilled packages certifying that Skilled was to pay Pilkington monies. Skilled then delivered notices of dispute in relation to the final certificates and Skilled and Pilkington engaged in the dispute resolution procedures mandated in the agreed terms, although Skilled did not seek to enforce its alleged contractual claims against Pilkington in litigation. Skilled also pursued claims against Pilkington under the Building and Construction Industry Security of Payment Act 2002 (Vic) (the 'SOP Act') and obtained adjudication determinations in its favour.

Issues in dispute

In 2010, Skilled commenced proceedings against CSR and Pilkington in the Supreme Court of Victoria. Skilled contended in the litigation that subcontract documents were never executed because it and Pilkington had never agreed on the dates for practical completion or separate liquidated damages milestones. Skilled argued that these issues were fundamental and that the correct legal analysis was that it and Pilkington had not entered into subcontracts at all and that CSR as owner of the plant had been unjustly enriched as a result of the works performed by Skilled.

Skilled said that these matters entitled it to a quantum meruit from CSR and the return of the bank guarantees from Pilkington.

CSR resisted Skilled's claim on the basis that a claim for unjust enrichment was unsustainable in circumstances where CSR was in a contractual relationship with Pilkington and Pilkington had engaged Skilled under separate subcontracts to which CSR was not a party. CSR relied on *Lumbers v W Cook Builders Pty Limited*[2] and *MacDonald Dickens & Macklin v Costello & Others*[3] as setting out the relevant principles.

Pilkington resisted Skilled's claim for the return of the bank guarantees on the basis that it had a contractual right to hold the guarantees. Pilkington also counterclaimed against Skilled seeking the monies certified as payable in the final certificates and contended that Skilled was estopped from asserting that subcontracts had not been entered into.

The proceeding was set down for hearing on a number of questions, which raised the following issues:

- the existence or otherwise of binding subcontracts for each of the Skilled packages;
- whether an estoppel would arise in Pilkington's favour if binding subcontracts had not been entered into;
- whether the agreed terms required that payment be made under a disputed final certificate; and
- the viability of the quantum meruit claim against CSR.

Existence of subcontracts

Notwithstanding the absence of formal execution, a binding and enforceable contract can arise by implication provided that the evidence supports an inference that the parties objectively agreed by their conduct to act on an agreement that included all of the essential terms. The Court noted the Victorian Court of Appeal decision in *PRA Electrical Pty Ltd v Perseverance Exploration Pty Ltd and Anor*[4] as a recent example of such a case.

The key questions for the Court were:

- had all of the essential terms been agreed?; and
- would reasonable people in the position of Skilled and Pilkington objectively think that there were concluded subcontracts?

The Court analysed whether the matter came within one of the three classes of case that were expressly referred to by the High Court of Australia in *Masters v Cameron*[5] or within what is frequently described as the 'fourth class' of case that was first considered by the High Court in *Sinclair Scott & Co Ltd v Naughton*[6] and subsequently applied by McClelland J in *Baulkham Hills Private Hospital Pty Ltd v GR Securities Pty Ltd.*[7]

The four classes of case concern parties who reach agreement on terms of a contractual nature but contemplate that the subject matter of the negotiations will be dealt with by a formal contract. The four classes are summarised below:

1. the parties have finalised the terms of their bargain and intend to be bound immediately, but propose documenting the bargain in a form that will be fuller or more precise, but not different in effect;
2. the parties have agreed all the terms of their bargain but have made performance of one or more of the terms conditional on the execution of a formal document;
3. the parties do not intend to make a concluded bargain at all, unless and until they execute a formal contract; and
4. the parties intend to be bound immediately and exclusively by the terms that they have agreed, while at the same time expecting to make a further contract in substitution for the first contract that contains additional negotiated terms.

After considering the evidence, the Court formed the view that the case fell within the fourth category and that binding subcontracts were entered into between Pilkington and Skilled by early May 2008, which were intended to operate both prospectively and retrospectively.

Save for the dates for practical completion and the separate milestones, the subcontracts were otherwise complete by this time and Skilled had expressly stated to Pilkington in correspondence on 15 May 2008 that: '[d]espite the fact that we've agreed that we're operating under the terms of the relevant Australian Standard (as modified by the agreed special conditions) I can't get signatures on the contracts until we've clarified these dates.' The Court found this to be an admission. Justice Vickery also found that the initial subcontracts were intended to operate for a reasonable period of time to allow the dates for practical completion and the separate milestones to be agreed and that, once those dates were agreed, the envisaged substituted agreements would replace the initial contracts and be executed.

In relation to the issue of whether there is in fact a 'fourth class' of case, it is relevant to note that a number of judges in a variety of jurisdictions have subsequently accepted the analysis of McLelland J in *Baulkham Hills*. The fact that there has been some academic suggestion to the contrary received short shrift in *Helmos Enterprises Pty Ltd v Jaylor Pty Ltd*,[8] where Chief Justice in Equity Young (with whom Hodgson JA and Stein AJA agreed) stated at paragraph 69:

> 'There has been recent academic discussion as to whether there really is a fourth class to be added to the three specified in *Masters v Cameron*; see the article in (2004) 20 *JCL* 156 by Peden, Carter and Tolhurst, "When three just isn't enough". However, an article by academics which attacks the considered view of MH McLelland J, one of the greatest equity judges of the 20th century, in a decision which was upheld in the Court of Appeal and since followed by almost every judge of the Court of Appeal and the Equity Division, as not being of any authority and contrary to what the High Court said in *Masters v Cameron*, does not rate serious consideration. Indeed no-one gave it more than passing reference in the instant case.'

After reviewing the evidence, the Court found that agreement on the original dates for practical completion for all three of the Skilled packages could be objectively inferred by 13 May 2008. Emails passing between Skilled and Pilkington together with internal Skilled emails supported this and Skilled had subsequently made a number of extension of time claims between 15 May and 23 July 2008 that proceeded on the basis that there had been identified original dates for practical completion. While Skilled's extension of time claims used the words 'proposed subcontract', the Court did not consider that this told against the objective evidence that subcontracts had been concluded. Significantly, the dates used by Skilled were also used by the superintendent in his claims assessments.

As to the separate milestone dates, the Court found that emails between Skilled and Pilkington together with internal Skilled emails objectively indicated that the dates for two of the three Skilled packages had been agreed by 20 May 2008. While there was no evidence of agreement having been reached on a separate milestone date for the third package, Pilkington and Skilled elected to treat the adjusted dates for practical completion as the sole trigger for liquidated damages so the separate milestone did not have the character of an essential term.

The Court also found that other conduct – including the submitting of progress claims, variation claims, final claims, claims for back charges and claims for liquidated damages, together with correspondence that invoked contractual provisions – pointed towards concluded agreements having been reached, as did the issue of final certificates by the superintendent and the fact that Skilled and Pilkington participated in the contractually mandated dispute resolution processes.

On the other hand, the fact that Skilled had pursued SOP Act applications against Pilkington was found to be of no assistance in determining the existence or otherwise of binding subcontracts because the definition of 'construction contract' in section 4 of the SOP Act has been modified to take it beyond the traditional concept of a common law contract by using the following words: 'construction contract means a contract *or other arrangement* under which one party undertakes to carry out construction work, or to supply related goods and services, for another party' [emphasis added].

Estoppel

The Court's finding in relation to the existence of subcontracts meant that it was not strictly necessary to deal with the issue of estoppel. The Court nevertheless decided to deal with the issue, for the sake of completeness, and found that Skilled would be estopped from denying the existence of binding subcontracts between it and Pilkington. The relevant category of estoppel was estoppel by conduct as described by the High Court in *Thompson v Palmer*[9] and *Grundt v Great Boulder Pty Gold Mines Ltd*.[10]

The Court did not accept an argument by Skilled that it was not possible for a party to be estopped from denying the existence of a nonexistent contract, and found that the evidence established the following propositions:

- Pilkington assumed there were subcontracts on foot for the Skilled packages in accordance with the agreed terms;
- Skilled induced Pilkington by its conduct to adopt this assumption;
- Skilled knew that Pilkington was acting on the assumption and intended that to be the case;
- Pilkington both acted and abstained from acting in reliance on the assumption; and
- departure from the assumption would produce detriment that would make it unconscionable

for Skilled to be permitted to depart from the assumption.

The Court found that equity required Skilled to be held to the assumption because Pilkington would otherwise be deprived of the benefit of the agreed terms in circumstances where Pilkington was obliged to deliver the works the subject of Skilled packages to CSR under its contractual arrangements with CSR.

Payments due under final certificates

It was common ground between Pilkington and Skilled that the superintendent had issued final certificates and that Skilled had delivered notices of dispute in relation to those final certificates within the required timeframe.

The competing arguments of Pilkington and Skilled were relatively simple: Pilkington argued that, unless and until the final certificates were overturned in arbitration or litigation, Skilled was obliged to make the payments due under the final certificates. Skilled, on the other hand, argued that the delivery of a valid notice of dispute deprived the final certificates of the evidentiary effect that they would otherwise have under clause 42.8, thereby 'neutralising' the final certificates.

The Court rejected Skilled's argument and found that the correct analysis was that there was a contractual obligation to make the payments certified as due under the final certificates unless and until the final certificates were successfully impugned in arbitration or litigation or the issue was otherwise resolved in a binding settlement agreement. The Court also noted that the requirement that payment is to be made on a superintendent's certification in the context of AS 2124-1992 was consistent with the decision of Gillard J in *Novawest Contracting Pty Ltd v Taras Nominees Pty Ltd*.[11]

While the agreed terms did contain modifications to the standard form AS 2124-1992, it is submitted that the modifications were of little relevance to the argument before the Court. It follows that the Court's judgment is also relevant to disputes arising under the standard form AS 2124-1992. It is also submitted that the decision is relevant more broadly to the important issue of the weight that the courts are likely to accord to a certificate issued by a superintendent under a construction and engineering contract.

Skilled's quantum meruit claim against CSR

In circumstances where binding subcontracts were found to exist and there was an undisputed contractual relationship between CSR as principal and Pilkington as contractor, Skilled's quantum meruit claim against CSR was dismissed based on the principles in *Lumbers v W Cook Builders*. In view of the decision of the Court of Appeal in *MacDonald Dickens & Macklin v Costello*, it appears very likely that the same result would have followed in England.

For the sake of completeness, it is noted that the Court's judgment in *Skilled Group Ltd v CSR Viridian Pty Ltd & Anor* was not the subject of any appeal.

Notes

1 [2012] VSC 290.
2 (2007) 232 CLR 635.
3 [2011] 3 WLR 1341.
4 (2007) 20 VR 487.
5 (1954) 91 CLR 353.
6 (1929) 43 CLR 301 at 317.
7 (1986) 40 NSWLR 622.
8 [2005] NSWCA 235.
9 (1933) 49 CLR 507.
10 (1937) 59 CLR 641.
11 [1998] VSC 205.

Andrew Laird practises as a barrister and mediator and is based in Melbourne, Australia. He appeared as counsel in this case for Pilkington Engineering Pty Ltd. He can be contacted in relation to this article at **andrewlaird@vicbar.com.au**.