Article 22 provides that before the consumer is bound by the contract or offer, the trader shall seek the express consent of the consumer to any extra payment in addition to the remuneration agreed upon for the trader's main contractual obligation. If the trader has not obtained the consumer's express consent but has inferred it by using default options which the consumer is required to reject in order to avoid the additional payment, the consumer shall be entitled to reimbursement of this payment.

Finally, note should taken of art.27, which although not mentioned in art.17 would appear to apply to all contracts within the scope of the Directive. Article 27 reinforces the prohibitions against inertia selling contained in Directive 2005/29 (Unfair Commercial Practices Directive) and provides that in such cases, the absence of a response from the consumer following such an unsolicited supply or offer of a supply shall not constitute consent. The Unsolicited Goods and Services Act 1971 (as amended) does not have a provision specifically to this effect, but in practice the detailed provisions as to positive acceptance by the person to whom the unsolicited goods or services have been offered or sent amounts to the same thing. There is probably no need for a specific amendment of the legislation, particularly as in any case most unsolicited offers will fall foul of the provisions in the Directive relating to Distance Contracts.

Construction of commercial contracts

1–9 Finally, it is desirable to conclude this chapter with a discussion on the approach which the courts in the UK adopt to the construction of commercial contracts. These are points which need to be borne in mind by the draftsman in dealing with any of the contracts covered within this book.

The classic approach of the common law is to construe a contract according to the plain and ordinary meaning of the words contained in it, without reference to extraneous circumstance such as the prior negotiations or intentions of the parties, except in the specific instance where a claim of rectification is being made to correct a manifest error in the contract.

This approach has been somewhat altered as a result of a number of key decisions.

In *Charter Reinsurance Co Ltd v Fagan* [1996] 2 W.L.R. 726, the House of Lords held that a provision providing that a reinsurer had to pay out to the insurer for the "sum . . . actually paid in settlement" did not mean that the reinsurer was only liable to pay what the insurer had actually paid. All it meant was that the amount the reinsurer had to pay was to be calculated by what the insurer was legally obliged to pay. In this decision, the court chose to interpret a term in the contract in a way which it felt better implemented the intention of the parties even though it perhaps went beyond the plain and ordinary meaning of the word "actually".

Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd [1997] 2 W.L.R. 945, HL considered the question of whether it is possible for a notice to be valid even though its form and content is defective in certain respects when compared with the requirements of the relevant notice clause. It is authority for the proposition that a notice will be held to be valid despite such defects, if there is clear evidence that the party on whom it was served understood, or ought reasonably to have understood, its contents.

In *Mannai*, a tenant served a notice to terminate which contained the wrong date of termination. The correct break date was January 13, 1995 and the notice specified January 12, 1995. The House of Lords held that the notice was valid as any reasonable landlord would have understood what was meant by it and when the break clause was to be exercised. Lord Steyn said, "If a notice unambiguously conveys a decision to determine, a court may nowadays ignore immaterial errors which would not have misled a reasonable recipient." Lord Clyde said, "The standard of reference is that of the reasonable man exercising his common sense in the context and the circumstances of the particular case . . . The test is an objective one . . . the actual understanding of the parties is beside the point."

In *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 W.L.R. 896 HL, the court went further in this approach. The case concerned the interpretation and effectiveness of a clause whereby certain investors assigned to the Investors Compensation Scheme any rights they might have against third parties in respect of negligent advice, including the West Bromwich Building Society. Lord Hoffmann described the principles of interpretation of documents under the common law as follows:

> "Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having 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 . . . subject to the requirement that it should have been reasonably available to the parties . . . [the background] includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man. . . . The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification . . . the meaning which a document would convey to a reasonable man is not the same thing as the meaning of its words . . . the meaning of the document is what the parties using these words against the relevant background would reasonably have been understood to mean . . . The rule that words should be given their "natural and ordinary meaning" reflects the common sense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude that something must have gone wrong with the language, the law does not require judges to attribute to the parties an intention which they plainly could not have had."

The principles in these cases were followed and approved in *Atari Corp (UK) Ltd v Electronics Boutique (UK) Ltd* [1998] 2 W.L.R. 66 in the Court of Appeal. The case concerned the interpretation of a fax purporting to exercise a right to reject goods supplied on sale or return. The court stated that the principles in *Mannai* could apply to contracts for the sale of goods and that "reading the fax in a common sense commercial way" the plaintiff must have understood that the defendant was rejecting the goods.

In *Dukeminster (Ebbgate House One) Ltd v Somerfield Properties Co Ltd* [1997] 2 E.G.L.R. 125, the Court of Appeal construed a rent review clause, which operated on the basis of a valuation of notional premises. The court said that valuation of notional premises operated in the real world and not in one of fantasy. Thus in the absence of clear words, notional premises cannot be taken to be such as would produce a valuation, whether it be too low or too high, which cannot reasonably have been intended to apply to the actual premises. The court relied on background evidence as to the lack of actual comparables for leased property and decided that the wording was intended to achieve a market rent, even though there were no comparables, and was not intended to allow the landlord to achieve a rent above the market value. It therefore construed the clause so as to give effect to this intention, and wording was, in effect, inserted in the clause by the court to make this point clear.

Two cases which were decided shortly after *Mannai* and *Investors* showed signs that the Court of Appeal was somewhat reluctant to embrace Lord Hoffmann's approach in its entirety. These are *Scottish Power Plc v Britoil (Exploration) Ltd* (1997) 94 (47) L.S.G. 30 CA and *Total Gas Marketing Ltd v Arco British Ltd* [1998] 95 (5) L.S.G. 28. In *Scottish Power*, Lord Staughton referred to the matrix of fact or the background against which the contract should be interpreted, but stated this should only comprise what the parties had in mind and what was going on around them when they entered into the contract. In *Total Gas*, the court proceeded on the basis of "the factual background known to the parties at the time at which [the contract] was entered into". Lord Gibson stated that he reached his decision "on the true construction of the letter of the contract". He did not adopt Lord Hoffmann's approach of good commercial sense which he said "was often like a chameleon, taking its hue from the environment". This decision was subsequently affirmed by the House of Lords (reported at [1998] 2 Lloyd's Rep. 209).

However, these two cases have not created any lasting impression., or, at any rate appear to have been interpreted as having been based on the same general principles as those set out in *Mannai* and *Investors*.

In *Halifax Plc v Gould & Swayne* [1999] P.N.L.R. 184, the Court of Appeal considered *Scottish Power*, but in fact approached the construction of the contract along the lines in *Investors*, having regard to the factual matrix, and in particular the general collaboration between the parties, in construing the relevant contract.

The same approach was evident in *Jolley v Carmel Ltd* [2000] 3 E.G.L.R. 68, where the Court of Appeal considered *Total Gas*. This case concerned a contract for the sale of land subject to a clause in the contract that the purchaser would apply for planning consent for a residential development on the site within three months and that completion would follow the grant of the same. Although the vendor made the application, two years or so later the purchaser had not obtained the consent and the vendor sought a declaration that the contract had been rescinded. The trial judge held that there was an implied term that the purchaser would make reasonable efforts to obtain planning consent within a reasonable period of time and that what amounted to a reasonable period of time would depend upon the circumstances at the time. He further held that the purchaser was not in breach of the implied term. The vendor appealed contending that the judge had erred in failing to apply previous authorities (in particular *Re Longlands Farm* [1968] 3 All E.R. 552 and *Total Gas*) and that he should not have construed the contingent condition of applying for planning permission in combination with an implied promissory obligation to proceed using reasonable efforts. The appeal was dismissed. The Court of Appeal stated that a decision of the court in relation to a specific contract did not create a precedent unless, as happened only rarely, the factual matrices

and the contractual terms were identical. The fact that *Longlands* had been approved in *Total Gas* did not, therefore, have any binding force save for the general principle that commercial contracts should be construed in a practical and realistic manner. The facts in the instant case were materially different from the two cited authorities and the trial judge could not be criticised for construing the contract so as to make the best commercial sense.

The principle in *Mannai* was further extended in *R. v East Sussex CC Ex p. Reprotech (Pebsham) Ltd* [2001] Env. L.R. 14, where an informal statement as to planning permission given by a planning officer was taken to bind the council since it was a "clear written indication" issued by their authorised representative.

Mannai and *Investors Compensation Scheme* have been widely considered, followed and applied in numerous cases up to the present. However, it important to stress that the application of the principles in *Mannai* and *Investors* are subject to certain limitations. They cannot be pushed too far.

In relation to *Mannai*, arguments as to the plain and ordinary meaning of a notice will have no effect on its validity, if it is required to comply with some statutory regime as to its form and content and fails to do so. In that event, the notice is invalid even if the recipient understands perfectly what is intended by it. (See *Sabella Ltd v Montgomery* [1998] 09 E.G.L.R. 153, which concerned a notice served pursuant to s.25 of the Landlord and Tenant Act 1954, which failed to comply with the relevant statutory instrument prescribing the form and content of such notices, and was therefore invalid.)

The conflict between issues of "plain and ordinary meaning" as opposed to "compliance with statutory requirements" can be seen working in *Garston v Scottish Widows Fund and Life Assurance Society* [1998] 3 All E.R. 596, CA, where a tenant served a contractual notice to trigger a break clause and a statutory notice requesting a new tenancy for the same premises. Both notices erroneously treated the date of grant of the lease as the date of its commencement, as opposed to the true date on which the term commenced. The court held that the statutory notice was invalid, but that the contractual notice was effective to terminate the existing lease.

Mannai was followed in *York v Casey* [1998] E.G.C.S. 26, CA (misdescription of the nature of a notice was not fatal as its nature was clear from its contents); *Havant International Holdings Ltd v Lionsgate (H) Investment Ltd* [2000] L.&T.Rev. 297 (obvious misdescription of person purporting to serve notice, when recipient really understood the true identity); *Ravenscroft Properties Ltd v Hall* [2001] EWCA Civ 2034, CA (obvious error of date on which notice period started to run not fatal); *Westminster City Council v HSBC Bank Plc* [2003] EWHC 393, QBD (T&CC) (service of a schedule of dilapidations held to be understood as a notice effective to trigger liabilities under a covenant to reinstate leasehold property); *Lay v Ackerman* [2004] EWCA Civ 184, CA (misdescription of landlord did not invalidate notice, even if the misdescription was intentional); *Lancecrest Ltd v Asiwaju* [2005] EWCA Civ 117 (a defective counter-notice in rent review proceedings was not fatal to its validity as it was clear what the tenant had intended); *Maurice Investments Ltd v Lincoln Services Ltd* [2007] 1 P. & C.R. 14 (how would a reasonable tenant have received a notice purporting to start a rent review process); *Rennie v Westbury Homes (Holdings) Ltd* [2007] EWHC 164 (upholding a notice to extend an option period); *Green v Westleigh Properties Ltd* [2008] EWHC 1474, (QB) (despite deficiencies in the drafting there was no doubt as to the purport of the notice delivered); *Bethell Construction Ltd v Deloitte and Touche* [2010] EWHC 3664 (Ch) (solicitor's letter determining agreement for extension of time was valid although defectively drafted since any reasonable solicitor with knowledge of the case receiving that letter must have construed it as operating to determine the agreement for an extension of time) and *Re Dunstans Publishing Ltd* [2010] EWHC 3850 (Ch) (transfer notice, issued by the partner of a deceased company shareholder in which she transferred his shares to herself, was valid and enforceable since it complied with the requirements in the Articles and a reasonable person would have understood the intent of the notice).

Charman v New Cap Reinsurance Corp Ltd [2003] EWCA Civ 1372 considered *Mannai* in relation to notice to terminate a contract of insurance, and is one of the decisions which shows that the principles in that case cannot be pushed too far. Charman appealed against a decision that a three-year reinsurance contract had ended after the second year. The contract contained a clause which enabled New Cap to raise the premium if there was a material change of circumstances or any "extraordinary claims developments". At the end of the first year, New Cap purported to terminate the contract, without any reference to the review clause, and Charman brought proceedings to enforce the contract. The defence was that an extraordinary claims development had occurred, in the second year, that New Cap had been entitled to invoke the premium review clause and that as no new premium had been agreed, the contract had lapsed after the first year. The Court of Appeal applied *Mannai* and held that the clause had not been invoked. The significance of the clause rendered it particularly important that Charman knew of New Cap's reliance on the clause and the reason for its invocation. It could not be accepted that what was said at the end of the first year about extraordinary claims developments was to be understood, and was understood, as invoking the clause on the ground of developments during both the first year and the second.

Further instances of decisions which turned on failure to comply with statutory requirements, as in *Sabella*, can be found in *John Lyon's Free Grammar School v Secchi* [1999] 3 E.G.L.R. 49, CA and *Speedwell Estates Ltd v Dalziel* [2001] EWCA Civ 1277, CA. However, this can sometimes prove a blessing in disguise. In *Barclays Bank Plc v Bee* [2001] 37 E.G.L.R. 153, CA, Barclays (Bee's tenants) appealed against a decision that a notice, served on Barclays by Bee, and opposing the grant of a new tenancy pursuant to the Landlord and Tenant Act 1954, s.25, was valid. Bee had previously sent two notices to Barclays in error, one of which opposed the tenancy without stating the grounds, and one which stated that the tenancy would not be opposed. Realising their error, Bee had then sent another notice to Barclays opposing the tenancy and stating the grounds for that opposition. Barclays contended that the second notice in which the tenancy was not opposed remained valid, since the first notice opposing the new tenancy was rendered invalid through the failure to state the grounds for opposition. The Court of Appeal set out a two-stage process to ascertaining the validity of a notice: (1) a consideration of what, on its true construction the notice says; and (2) a consideration of the requirements for that notice and whether the notice met those requirements. In the first stage of the process, *Mannai* will apply. The Court of Appeal held that Bee was entitled to rely on the third notice opposing the grant of a new business tenancy since neither of the first two notices were valid. The first notice opposing the tenancy was not valid because it failed to comply with statute by stating the grounds for opposition. However, the second notice agreeing to the tenancy (even though it complied with the

statute) was clearly inconsistent with the first opposing notice. Thus the second notice was invalid as well under the principles in *Mannai*, since (with two conflicting notices) it would have been impossible for the recipients to ascertain the landlord's intentions. This left only the third notice, whose terms were clear and overrode the first two notices, and which also complied with the statute.

This case should be distinguished from the more recent decision in *Saxon Weald Homes Ltd v Chadwick* [2011] EWCA Civ 1202 discussed below. The Court of Appeal in *Chadwick* stated that *Barclays Bank Plc v Bee* was to be distinguished since in that case a single letter sent to a tenant from his landlord contained contrary notices as the termination of a tenancy and the grant of a new tenancy. This was different from the present case where the relevant letter was sent subsequently and distinctly from the previous letter and notices on which the landlord was now attempting to rely.

A further application of these principles can be seen in *Lemmerbell Ltd v Britannia LAS Direct Ltd* [1998] 3 E.G.L.R. 67, CA, *Proctor & Gamble Technical Centres Ltd v Brixton Estates Plc* [2002] EWHC 2835, Ch D and *Hexstone Holdings Ltd v AHC Westlink Ltd* [2010] EWHC 1280 (Ch). In *Lemmerbell* a notice was held to be invalid since serving the notice on and by incorrect parties was not an obvious slip, and the error was not apparent. In *Proctor & Gamble* a notice was served to trigger a break clause in a lease. It was served by the original tenant rather than another company in the same group to which the lease had subsequently been assigned. It was held that the original tenant had acted on the assignee's behalf and that the effect of the notice was to give unambiguous notice of an intention to exercise the break clause, notwithstanding the error. However, the notice was invalid, as it was not obvious on its face who was the current lessee. As the landlord knew that the original tenant retained an interest in the property following the assignment, it was possible that a further, unauthorised, assignment had taken place. In *Hexstone* it was held that a notice to terminate an underlease was invalid because it had been given by the parent company of the tenant and there was no evidence that the parent company had authority to act as agent on behalf of the tenant.

From the above authorities, it appears that *Mannai* cannot rescue a statutory notice where there is incorrect or missing information prescribed by statute or where a statutory notice is not in the prescribed form. A recent example of this approach can be found in *Hopkins v Beacon* [2011] EWHC 2899 (Ch). The claimant filled in the standard Land Registry form dealing with objection to an application for registration of title by adverse possession. He ticked the objection box on the form but not the counter-notice box requesting that the objection be dealt with under the procedure in the Land Registration Act 2002 Sch.6 para.5 (which would require the applicants to prove that they reasonably believed that the land had belonged to them for more than 10 years). The failure to tick the counter-notice box did not automatically mean that the procedure had not been invoked, since it could not be said that ticking this box was a mandatory requirement. However, it was necessary to consider (on the basis of the test in *Mannai*) whether a reasonable land registrar receiving the form and attached documents would have been left in any doubt that the procedure had been requested. On the facts and considering the form and attached documents the Court found it was reasonable for the registrar to assume that, as the counter-notice box had not been ticked, the complainant did not wish to invoke the procedure.

This is particularly so given that (under cl. 2.2.3) the contractor offers to take on proper additional liabilities if he is awarded the system contract.

In some cases, the customer will agree with the contractor that, following the definition study and the creation of the specifications, the system contract will be put out to competitive tender to a number of contractors (including the contractor) based upon the specifications. Public authorities, for instance, are now required in many cases to put such contracts out to competitive tender under public procurement directives of the European Union. These directives may also constrain the customer in the instructions he gives to the contractor who draws up the specifications. For instance, he will not be able to permit the contractor to specify proprietary equipment which only that contractor can supply. To do so would be to prevent, in effect, other contractors from tendering, because they could not comply with the specification as drawn.

Where this procedure is agreed, it may be appropriate to vest ownership of the specifications in the customer, or at least for the contractor to permit their use in the manner contemplated. In either event cl. 7 would be modified accordingly. However, if this occurs, cl. 8 is doubly important, because if the contractor does not win the tender, then the winning contractor and the customer should apportion the risk of inaccuracy in the specifications between them as they see fit. The contractor who drew them up should not take this risk, given that he will enjoy none of the profits of the system contract, and be unable to take advantage of the exclusion clauses (if any) built into it.

In these circumstances, the contractors should also seek an indemnity from the customer against third-party claims in respect of inaccuracies in the functional specification and the system design specification, particularly from the successful tenderer who wins the system contract, and from his sub-contractors. Clause 6.3 of Precedent 3.2 in Ch.3, should be used, suitably adapted, and reference should be made to the discussion on that clause in that chapter.

Precedent 4.2

4–3 Having created and approved the functional specification and the system design specification for the system, the parties are in a position to negotiate the price and the timescales for its supply under the terms of the system contract set out as Precedent 4.2. Precedent 4.2 is a complicated and extensive document and is probably best analysed clause by clause.

Clause 1 lists the principal definitions used in the contract. It builds upon the definitions used in Precedent 4.1. The operation of the contract is tied to three defined specifications, for the function of the system, for the design of the system, and for the civil works needed to make the site ready for the installation of the system. The other definitions support and interwork with these three main definitions and are all to some extent interrelated. No changes should be made to any one of the definitions without considering the impact of the change on other definitions.

Clause 2 lists the basic obligations of both parties. The contractor supplies the system in accordance with the contract and the customer pays the agreed price.

Clause 3 deals with the passing of ownership and risk. It should be noted that the provisions in this clause would not be acceptable to many customers, particularly given the schedule of payments set out in cl. 6. Many customers require property to vest in

equipment as it is delivered to site, or even, where advance payments are made, as it is constructed in the contractor's factory.

Clause 4 provides detailed provisions dealing with the apportionment of liability for loss, damage, death and personal injury caused during the course of the contractor's performance of the contract (including while on the customer's premises in the warranty period). The provisions of s.2(1) of the UCTA have no application, except in the unlikely event that the customer is a natural person. Where this is the case, appropriate provisions providing unlimited liability for death or personal injury caused to the customer by the contractor's negligence should be added.

The price and payment terms in cll. 5 and 6 are of the utmost importance to the contractor. Particularly crucial is to obtain a payment schedule which at least keeps pace with, if it is not in advance of, the cash spent by the contractor in the performance of the contract. It is not sufficient for the contractor to negotiate a favourable contract price if the payment terms are so unfavourable that poor cashflow causes the contractor to lose all his profit in interest payments to his bank. The payment clause is linked to cl. 25 which deals with variations to the contract—all but the most straightforward system supply contracts nowadays tend to work on the basis of a fixed element and variable elements.

Clause 7 should be read in conjunction with cl. 6 too. Many long-term contracts require price adjustment clauses if the fixed price is not to be rendered unprofitable in the course of performance. Clause 7 deals not only with inflation or the fluctuation in material prices, but also with increased costs due to changes in legislation, or factors within the control of the customer. In the UK, inflation is currently less of a problem than in the past, but system contracts can often stretch over a number of years, in which case even modest inflation rates can eat into profits. In any event the other causes of cost increase are still an issue. In other countries, where inflation is much higher, such clauses are absolutely vital.

The provisions of cl. 7 use examples of various indices and percentages, but, in practice, these, and indeed the actual terms of the clause, will have to be adjusted to deal with the particular issues on escalation affecting each contract.

Clauses 8–11 deal with the delivery schedule and the consequences of delay, including a liquidated damages clause. It is important that both parties are given notice of any potential slippage in timescale, while there is still the possibility for remedy (cl. 10). Where no timescale is set, the contract will contain an implied term that it is performed within a "reasonable time" (s.14(1) of the Supply of Goods and Services Act 1982 (SGSA)) although the parties are likely to have a different view as to what constitutes a "reasonable time" (see, e.g. *Astea (UK) Ltd v Time Group Ltd* [2003] EWHC 725 (TCC)). Accordingly, it is sensible to set out timescales throughout the life of the contract particularly where the contract is to be performed in stages. A liquidated damages clause generally imposes an obligation upon one party to a contract to pay to the other a sum of money in the event of the first party's breach. Another possibility is a clause which allows the aggrieved party to withhold or set off sums of money owing to the party in breach, either under the relevant contract or as a result of some other transaction between the parties. If the court accepts that (at the time the contract was made) the sum in question was a genuine pre-estimate of the loss that would be suffered by the other party in the event of the breach, then the aggrieved party can recover the sum in question without proving the actual loss suffered.

If it can be shown the sum in question is not a genuine pre-estimate of loss, then two possibilities arise. If it is larger than any loss that could be suffered as a result of the breach in question, then the court will regard it as a penalty. This will also be so if one sum is specified whatever the nature of the breach and however minor. This is particularly the case where set-off or withholding clauses allow the aggrieved party to keep back all sums owing irrespective of the severity of the breach that has occurred. The question as to whether a clause provides for liquidated damages or a penalty has to be considered as a matter of construction of the particular contract taking account of all the facts of the case, and judged at the time the contract was made, not at the time of the breach.

However, if it can be shown that the sum in question is less than the likely loss arising from the breach, it will be generally assumed that the parties had this situation in contemplation and that the clause is actually not meant to provide compensation or impose a penalty, but instead to act as a limitation of liability. (See *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] A.C. 79 HL; *Cellulose Acetate Silk Co Ltd v Widnes Foundry (1925) Ltd* [1933] A.C. 20 HL; and *Imperial Tobacco Co v Parslay* [1936] 2 All E.R. 515).

There is no doubt that in many trades (for instance the building industry) such clauses have come to be regarded as having some of the characteristics both of liquidated damages and limitations of liability rather than penalties. See, for instance, *Hall v Van Der Heiden* [2010] EWHC 586 (TCC) (a figure of £700 per week claimed as liquidated damages was a genuine pre-estimate of loss, which took into account the costs of alternative accommodation and other charges incurred whilst the claimant could not occupy the relevant property, and could not be described as a penalty) and *Azimut-Benetti SpA v Healey* [2010] EWHC 2234 (Comm) (clause entitling a yacht-building company to liquidated damages of 20 per cent of the full contract price in the event of the buyer's default was, on the facts and evidence, commercially justifiable and could not be construed as a penalty for breach of contract).

Such clauses are of course of benefit to both parties, since the customer has a ready remedy, and the contractor has a cap to his liability for delay under the contract.

Clause 12 deals with that most difficult question of acceptance. Proper and simple methods of acceptance are vital to the contractor, because he is not discharged of his basic performance obligations under the contract until he has achieved acceptance. It follows that acceptance should come about as a result of compliance with objective, easily demonstrable criteria, and not as a result of persuading the customer that he should be satisfied with the contractor's performance. Clause 12 proceeds on the basis that the civil works and the system are all accepted at the same time by means of a series of acceptance tests that have been specified as a schedule to the contract. The key to the clause is cl. 12.2. The purpose of the tests is to demonstrate compliance with the relevant specifications and nothing else. If compliance is demonstrated, the customer must issue the acceptance certificate. This is obviously fair, given that, after the work carried out under the relevant definition study contract, compliance with the relevant specifications should be all that the customer requires. The model of this clause should always be used where there has been a prior definition study contract. Where this provision is used, and the acceptance tests are agreed in advance, the contractor knows what he has to satisfy, and there is little room for dispute.

However, acceptance tests which are designed to deal with vaguer issues, such as that the system is operating both in accordance with the specification and "to the satisfaction

of the customer", should be avoided. This is especially so when acceptance tests to meet such criteria are not agreed before the contract is signed, and attached as a schedule to it, but left to be negotiated between the parties during the course of the contract. Here the contractor is at the mercy of the customer, and acceptance becomes a matter of satisfying the subjective demands of the customer rather than demonstrating compliance with objective criteria. Such provisions are, in particular, completely inappropriate where there has been a prior definition study contract, because, as stated previously, the customer has had all the opportunity he needed at that stage to see that his various requirements and concerns were built into the functional specification. Once this has been dealt with, nothing remains for the contractor except to demonstrate that the system supplied delivers a performance in accordance with that functional specification. If it does, the customer should have no alternative but to accept it, since he is getting what he contracted for. Clause 12.4 deals with what happens if the system fails the acceptance test. In practice, particularly if the project has been ongoing for a long time, the customer may very well be reluctant to terminate for breach, and will want to give the supplier the opportunity for remedying the defect, without prejudice to its rights and remedies for breach of contract. The inclusion of the materiality qualification will prevent the customer from refusing acceptance because of a minor irrelevant defect.

Clause 13 is an elaborate warranty, but its basis is again simply that of the obligations in relation to the various specifications to which performance of the contract is tied. Clause 13.1 provides the warranty that the contractor undertook to give in the definition study contract (cl. 8.2 of Precedent 4.1). Here the contractor now has to warrant that the system design specification specifies a system which will perform in accordance with the functional specification, and that the system he actually supplies complies with the system design specification. Additionally, the civil works, and individual components of the system, are warranted to comply with the relevant specifications, and there are some more general warranties in relation to these aspects of the contract relating to materials and workmanship and reasonable care and skill in carrying out work under the contract. These latter may be adjusted to cater for the particular contract, but it is hardly likely that the contractor will be able to contract out of them.

The remainder of cl. 13 is standard and self-explanatory, if somewhat detailed, but the definition of "Defect" needs mention. The defined term "Defect" relates only to those defects which the contractor is liable to remedy under the contract. The term "defect" (uncapitalised) bears its general meaning. This is why the term "defect" (uncapitalised) is used in cl. 13.3 in the provisions relating to exclusion of liability.

The matters relating to spare parts, support and consumables covered by cll. 14 and 15 are not part of the contractor's warranty obligations, but instead are chargeable items provided as a post-acceptance service. Such provision will require additional contract terms to be drawn up. This Precedent provides either for the use of the contractor's standard terms and conditions of sale, or for the use of specimen contracts which would be attached as schedules to the contract. The maintenance contract, for instance, would be along the lines of Precedent 3.1 and the support service could be entered into under a contract based on Precedent 3.2.

Termination under system contracts usually takes place for three reasons: breach, insolvency or convenience. Clause 16 deals with all three issues. Its provisions are necessarily complicated because it has to deal with the unravelling of a complex contract which, it is likely, will have been part performed at the date of termination. Either party has the right to terminate for breach, but only the customer can terminate for convenience. This latter issue should not bother the contractor, since the question of impossibility of performance for technical reasons will already have been considered and dismissed upon the successful performance of the relevant definition study contract.

Under cl. 16.4, where the customer terminates for breach or insolvency, he is entitled to recover his direct losses as a result of such termination, to have the contract performed by someone else, and to recover the additional costs of this course of action (if any) from the contractor. The provisions of cl. 16.4 are designed to put the customer in the position of being able to have the work performed elsewhere, and to take advantage (if he wishes) of the contractor's part performance, subject to a fair and reasonable payment.

On the other hand, cl. 16.5 enables the contractor who terminates for breach or insolvency of the customer, or who suffers a termination for convenience at the hands of his customer, to recover his lost bargain by charging cancellation charges which include an element of profit. Here cl. 16.7.1.3 should be noted, which provides for compensation for loss of profits and overheads on the uncompleted portion of the contract. Most contractors would regard this as fair, since full payment (even with profit element) of work completed to date (see cl. 16.7.1.1) does not take account of the lost opportunity cost of the contractor; he could have entered into another contract which he would have performed in full, but instead he concentrated his resources on the customer. Customers find it hard to resist this provision in cases of breach, but often try to do so when contemplating termination for convenience. Clause 16.7 also provides that the contractor, may, but is not obliged to, permit the customer to make use of work performed to date, subject to payment.

Special note should be taken of cll. 16.6 and 16.7.5. Whatever the circumstances of termination, the contractor should not permit copyright in software used on, or in the operation of, the system to fall into the ownership of the customer. These clauses provide that all such software remains subject to the relevant licence provisions set out in cl. 17, and that the customer must pay a licence fee for their use. Clause 16.7.5 goes somewhat further than cl. 16.6, in requiring a licence fee for all products, not just software. Such extension may have little practical applicability, but is justified (where it does apply) because under cl. 16.7 the relevant breach or termination is the responsibility of the customer.

Clause 17 deals with all of the issues in the contract relating to know-how and intellectual property rights. Clauses 17.1–17.5 inclusive deal with the question of the contractor's liability for claims that the system infringes third-party intellectual property rights. The same considerations as to breach of the warranties of good title and quiet possession arise under this system contract as under the conditions of sale in Ch.2, and the relevant discussions in Ch.1, and in Ch.2 in relation to cll. 5 and 10 of Precedent 2.1, apply. In this Precedent the option of warranting only such title as the contractor may have in relation to infringement of third-party intellectual property rights has been followed. Given the complexity of systems, and the possible unknown and unquantifiable exposures, this seems the safest course.

Clauses 17.6 and 17.8, continuing the principles of cl. 7 of Precedent 4.1, provide that ownership of the intellectual property rights in all items supplied under the contract, including the specifications and the system itself, remain with the contractor. This intellectual property is the contractor's most important resource for carrying on his business and for fulfilling future contracts with other customers. Although many customers will

seek to own at the least intellectual property generated or arising during the performance of work (e.g. special bespoke development work) under the contract, this should be resisted if at all possible. However, the customer does need certain rights to the contractor's intellectual property (particularly in relation to software) or he will not be able to use the system in the way that the contract intended. The contractor thus grants him suitable licences, in return for licence fees, and subject to suitable controls. Clause 17.7 deals with this and references the pre-agreed licence terms which are attached as schedules to the contract. These should be set out in some detail. In particular, the parties will need to decide whether or not the licence is exclusive. The supplier is unlikely to agree to an exclusive licence (although it may be possible, depending on the nature of the system, to agree on a grant of a licence to use the system as a whole but for non-exclusive licences to be granted in respect of individual components). The licence will also need to address questions such as whether it may be used by other companies in the customer's group (which should usually be acceptable to a supplier) and to associated or joint venture companies (which may be less acceptable); provisions for updates and modifications (if applicable) and access to source code. Finally, cl. 17.9 provides short-form confidentiality obligations binding both parties.

Clauses 18–21 inclusive are concerned with procedural matters and the general implementation of the work under the contract.

Clause 18 provides for the two parties to appoint project managers, who will administer and monitor the progress of the contract. In order for the parties to co-operate smoothly in the discharge of the contract, information, defined in the contract as Contract Implementation Information, needs to pass between them, for instance in relation to the state and condition of the site. Errors in such information can cause delays to the contract and extra expense. Clause 19 provides that the party receiving such information is entitled to rely on it (although he should point out errors if he notices them) and that he should be compensated for any costs incurred because of errors in it; additionally, where relevant, he should be granted an extension of time to take account of the time lost through acting on incorrect information. However, neither party should be responsible for damages at large for such errors. This is particularly important for the contractor, since he must take care that such information does not somehow become embodied in the specifications for which he is responsible under the contract. Clause 19.3 and the definition of "Contract Implementation Information" taken together obviate this danger.

Clauses 20 and 21 deal with both the carrying out of the civil works on the site where the system is to be installed, and the delivery, installation and commissioning of the system itself on the site. The definition of the "Works" comprises all of these matters. It should be noted that this Precedent is not as a whole suited to a situation where complex civil works are required, such as the building of a whole factory. The provisions in this Precedent are adequate to cover the supply of a system accompanied by minor civil works, such as the installation of an environmentally controlled area in which a computer system is to be installed, or the engineering works associated with installing a central heating and air conditioning system. Where more complex civil works are required, the standard JCT or RIBA contract forms should be used as appropriate. Since the customer is in control of the site, cl. 20 deals with the conditions for the contractor's access to the site, and how he will conduct the work on the site, while cl. 21 permits the customer to suspend and resume performance of the Works, subject to appropriate notice and compensation.

Clause 22 sets out the parties' obligations regarding migration of data. The customer, as a "data controller" as defined in s.1 of the Data Protection Act 1998 (as amended), must ensure that parties to whom it transfers "personal data" (as defined in s.1 of the 1998 Act) treat such personal data in accordance with the eight data protection principles set out in the Act. It will be liable for any default in doing so by the supplier. The customer might even consider seeking an indemnity from the supplier for any breach of its obligations in respect of the processing of the personal data.

Clauses 23 and 24, which deal with respectively training and documentation, will not apply in every case. An additional charge may be paid in respect of the provision of training and the schedule will need to set out who is to be trained, when, where and for how long.

Clause 25 sets out a procedure for contract variations. It is based on the principle that each variation may entail changes to the price, timescales and specifications of the contract, and that therefore no variation should be implemented until its effect on the contract has been assessed and all these matters agreed. Clause 25.6 is particularly important. If the customer insists on a variation which would give rise to a Defect (as defined, i.e. a defect (uncapitalised term) for which the contractor would be responsible under the contract) the contractor is under no obligation to implement such a variation, and if he does so may disclaim responsibility for the consequences of its implementation and exclude his relevant liabilities under cl. 13.1 (warranty). Following on from this concept, cl. 26 makes it clear that the customer is totally liable for the functional specification (as was contemplated by cl. 2.1.3 of Precedent 4.1).

Clauses 27–35 inclusive deal with those matters of general importance under the contract which are often referred to as boilerplate and are largely self-explanatory. The matters that they cover are dealt with in other ways in many of the other precedents in Chs 2 and 3, but the clauses used here are more detailed, given the importance and complexity of a system contract.

A few detailed points arise. It will be noticed that cll. 28 and 33 are general exclusion clauses. Clause 28 deals with economic loss, while cl. 30 is an entire agreement clause, drafted to deal with the issues raised and discussed in Ch.1–5.1, which also excludes implied warranties and representations, liability for negligent pre-contract misrepresentations and all legal remedies for breach other than those expressly provided under the contract. It will have been noted that, where clauses in the contract deal with a particular issue, they also include a provision limiting the liability of the contractor to the express remedies in the clause (see, e.g. cl. 17.5 in relation to infringement of third-party intellectual property rights). However, given the various issues which arise under the system contract and its complexity, the addition of general exclusion clauses as well is considered prudent.

The drafting of these general exclusion clauses takes account of the issues relating to blanket exclusion of liability under the UCTA discussed in Chs 1 and 2, by the inclusion of cl. 33.4.

Clause 28.2 is necessary because the remedies upon termination contained in cl. 16 do have an element of compensation for economic loss and, without the special provisions of cl 28.2, the general exclusion of economic loss under cl. 28.1 would conflict with these provisions.

Clause 29 deals in detail with events of force majeure; not only those which delay or make it impossible to perform the contract, but also those which make it more difficult or expensive to perform, but do not preclude performance altogether. Because of the complex nature of a systems contract, it is not possible simply to permit suspension of the contract. The two parties must try to work around the problem, and treat extensions to timescale, and increased costs, as contract variations to be dealt with under cl. 25.

Clause 31 deals with waiver and variation in a standard manner. Clause 31.2 prohibits all variations or amendments to the contract except in writing in the prescribed form. It is true that these clauses are of doubtful legal validity in that it is possible for the parties to agree to vary the contract by some different procedure (including an oral agreement). If the purported variation can be properly evidenced and is legally enforceable then it will have effect as varying not only the relevant parts of the contract, but also the variation procedure in cl. 31.2 itself. The real point about cl. 31.2 is that it lays down a procedure which the parties should follow as a matter of good contract management, and it makes it necessary for the party relying on any variation falling outside the clause to produce very strong evidence to rebut the presumption that the "variation" was in fact regarded by the other party as an informal concession and not legally binding.

Clause 34 is a notice clause which deals with the points about service of notice which were discussed in Ch. 2 in relation particularly to service by electronic means and the judgment in *Schelde Delta Shipping and Chartering BV v Astarte Shipping BV* [1995] 2 Lloyd's Rep. 249.

Finally, it should be noted that cl. 35 submits all disputes to the court for resolution after a period in which the parties try to solve the dispute themselves. Many system contracts favour the insertion of arbitration clauses, but in practice, in many cases, arbitration is more time consuming and expensive than litigation in court and with a less certain outcome. Also, one of the best methods of concentrating the minds of the parties to solve their problem is for them to realise that, at least in the absence of actual agreement at the time to put the matter in question to an arbitrator, the only way forward is to go to court. System supply agreements frequently contain an escalation procedure for the resolution of disputes and reference in this regard should be made to Precedent 17.3.

Precedent 8.3

Selective distribution agreement

This Agreement is made on the [ ] day of [ ] [ ] between [ ] Limited whose registered office is at [ ] (the "Principal") and [ ] Limited whose registered office is at [ ] (the "Distributor").

1 Definitions

1.1 The "Products" means those products listed in Schedule 1 [and such further products that the Principal may in writing permit the Distributor to distribute].

1.2 "The Reserved Territory" is comprised of those member states of the EU listed in Part 1 of Schedule 2 which are reserved by the Principal to operate that selective distribution system in respect of which the Distributor is appointed as Authorised Distributor pursuant to cl. 2.1

1.3 The "Distributor Territory" means that part of the Reserved Territory allocated to the Distributor in terms of clause 2.1 and listed in Part 2 of Schedule 2.

1.4 The "Trademark" means those trademarks and trade names listed in Schedule 3 [and such further trade marks or trade names that the Principal may in writing permit the Distributor to use in respect of the Products in the Territory].

1.5 The "EU" means the member states that from time to time constitute the European Union and the European Economic Area (the "relevant groupings"). For the avoidance of doubt if a state shall cease to be a member state of or shall become a member state of one of the relevant groupings it shall thereupon cease to be or become, as the case may be, part of that relevant grouping for the purposes of this definition.

1.6 The term the "Effective Date" shall bear the meaning set out in cl 12.1.

1.7 An "Authorised Distributor" means a reseller of the Products at the wholesale level of distribution appointed by the Principal in respect of any part of the Reserved Territory under a distribution agreement in identical terms to this agreement.

1.8 An "Authorised Retailer" means a reseller of the products at the retail level of distribution within the Reserved Territory satisfying the requirements for appointment as an authorised retailer for the Products from time to time specified by the Principal and who has been so appointed pursuant to an agreement entered into with the Principal or an Authorised Distributor.

1.9 "Distributor Requirements" means the requirements set out in Schedule 4.

2 Grant and terms of distributorship

2.1 The Principal hereby appoints the Distributor as an Authorised Distributor of the Products and hereby grants the Distributor (pursuant to such appointment) a licence to market distribute and sell the Products under the Trademark in accordance with and subject to the terms of this Agreement.

2.2 The Principal undertakes that during the continuance of this Agreement:

2.2.1 it will not appoint in the Distributor Territory any other distributor or reseller of the Products (whether or not an Authorised Distributor); and

2.2.2 it will supply the Products within the Reserved Territory only to Authorised Distributors except in any territory within the Reserved Territory in respect of which it has not appointed an Authorised Distributor on an exclusive basis, in which case it reserves the right to supply the Products to Authorised Retailers appointed in respect of that territory and to end users in that Territory.

2.3 The Principal undertakes to the Distributor that during the currency of this agreement it will within the Reserved Territory only appoint as Authorised Distributors those distributors who comply with the Distributor Requirements and that such appointments shall be made using agreements having substantially the same terms as this Agreement.

3 Responsibilities of distributor

3.1 The Distributor shall during the continuance of this Agreement diligently and faithfully serve the Principal as its distributor and shall use its [best][reasonable] endeavours to improve the goodwill of the Principal and to further and increase the sale of the Products.

3.2 The Distributor will ensure that it conforms with all applicable legislation rules regulations and statutory requirements from time to time in relation to the Products.

3.3 The Distributor undertakes [during the continuance of this Agreement] not to manufacture or sell in or import into the Distributor Territory any goods competitive with the Products and not to be interested directly or indirectly in any such manufacture sale or importation. [The obligations imposed by this clause shall continue until the expiry of a period of [five years] from the Effective Date provided that if this Agreement is terminated for any cause whatsoever prior to the expiry of such period then upon such termination such obligations shall cease immediately.

3.4 The Distributor shall leave in position and not alter cover or erase any notices or other marks (including without limitation details of patents or notices that a trademark design or copyright relating to the Products is owned by the Principal or a third party) which the Principal may place on or affix to the Products.

3.5 The Distributor will (for so long as this Agreement continues in force) comply with and satisfy the Distributor Requirements, and in particular undertakes to achieve targets in relation to the Products in accordance with paragraph 6 of Schedule 4.

3.6 The Distributor shall insure at its own costs with a reputable insurance company all stocks of the Products as are held by it against all risks that would normally be insured against by a prudent businessman to at least their full replacement value and produce to the Principal on written demand full particulars of that insurance and the receipt for the then current premium.

[**3.7** The Distributor shall provide to customers an after-sales repair and maintenance service in accordance with standards methods and procedures prescribed from time to time by the Principal. The documentation setting out the standard methods and procedures currently prescribed by the Principal is attached as Schedule 7 to this Agreement.]

4 Sales activities

4.1 The Distributor shall be free to sell the Products to any retailer or distributor who has been appointed as an Authorised Retailer or Authorised Distributor and to any person, other than a consumer or other end-user, outside the Reserved Territory but within the EU.

4.2 The Distributor shall not sell the Products outside or inside the EU except as provided in cl 4.1.

4.3 The Distributor shall at its own entire discretion determine the prices at which and (except as specifically provided in this Agreement) the terms and conditions on which it sells the Products.

4.4 Notwithstanding the provisions of cl 4.2, the Distributor shall be entitled to carry out general advertising or promotions in media or on the internet that reach potential purchasers to whom the Distributor is prohibited from selling the Products pursuant to cl 4.2 provided that such advertising and promotion is primarily intended to reach potential purchasers to whom the Distributor is authorised to sell the Products pursuant to cl 4.1 ("authorised customers") and that such advertising and promotion is a reasonable way to reach authorised customers.

4.5 The Distributor may appoint as an Authorised Retailer any retailer within the Distributor Territory which satisfies the retailer requirements set out in Part 1 of Schedule 8. Any such appointment shall be made using the Authorised Retailer Agreement set out in Part 2 of Schedule 8. If the Distributor receives a request for appointment as an Authorised Retailer from a retailer established outside the Distributor Territory it shall refer the request to the Principal. The Principal undertakes to the Distributor that it will only appoint as Authorised Retailers within the Reserved Territory retailers who comply with the retailer requirements set out in Part 1 of Schedule 8 and that such appointment shall only be made using the Authorised Retailer Agreement set out in Part 2 of Schedule 8.

5 Supply of the Products

5.1 The Distributor shall purchase all its requirements for the Products (ready packaged) either from the Principal or from any other Authorised Distributor or Authorised Retailer for the Products.

5.2 The parties hereto agree that orders placed by the Distributor with the Principal under cl 5.1 or for any other items shall be on the terms set out in Schedule 5.

5.3 The Principal reserves the right to improve or modify the Products without prior notice [provided that details of any modification affecting [form fit function or maintenance] [or] [any permissions consents or licences obtained by the Distributor pursuant to cl 12.4] shall be notified to the Distributor in which event the Distributor may vary or cancel any orders placed for the Products prior to the receipt of such notification except to the extent that these orders can be met by the supply of Products which do not incorporate the improvement or modification notified hereunder. Variation or cancellation hereunder shall be effected by the Distributor notifying the Principal thereof within fourteen days of receipt by the Distributor of the relevant notification of the relevant improvement or modification. The Distributor's rights of cancellation under this clause shall be its sole remedy in the event of any improvement or modification being made to a Product, and in particular, but without limitation, no compensation or damages for breach of contract shall be payable to the Distributor by reason of such improvement or modification].

6 Distribution records

6.1 The Distributor shall retain for at least one year duplicate copies of all invoices relating to sales of the Products by it, recording the date of sale and the name and address of the purchaser, and details of the relevant Products.

6.2 The Distributor shall retain for at least one year duplicate copies of all purchase orders for the Products placed by it on the Principal or any other person, recording the date of purchase and the name and address of the seller, and details of the relevant Products.

6.3 The Distributor shall in addition to the specific requirements of cll 6.1 and 6.2 keep all relevant accounts together with supporting vouchers (including without limitation copies of invoices) and other relevant papers relating to the business carried on by it in the Products under this Agreement.

6.4 The Distributor shall upon reasonable notice supply at any time to the Principal, upon request, details of persons who have sold to it and bought from it Products during the preceding 12 months, including names and addresses and the details of the relevant Products for each transaction.

6.5 The Principal shall have the right at any time upon reasonable notice to appoint an independent firm of chartered accountants (the "auditor") to audit and inspect all of the records referred to in this clause for the purpose of verifying the accuracy of any information given to it by the Distributor under cl 6.4 and otherwise for verifying that the Distributor is in compliance with its obligations under this Agreement provided that the auditor shall not disclose to the Principal details of the records concerned which shall remain confidential between the auditor and the Distributor and the auditor shall issue a certificate either stating that the information given under cl 6.4 is correct or that the Distributor is in compliance with its obligations under this Agreement as aforesaid, or stating that this is not the case and specifying details of the inaccuracies or the lack of compliance as the case may be.

6.6 Nothing in this clause or elsewhere in this Agreement shall entitle the Principal to pay regard to or monitor the prices at which the Distributor sells the Products.

7 Advertising and merchandising

7.1 The costs of all advertising and sales promotion activities shall unless otherwise decided be borne by the Distributor.

7.2 All advertisements point of sale promotion merchandising and publicity material for the Products issued by the Distributor shall be subject before issue to the prior approval of the Principal.

7.3 All sales promotion activities carried on by the Distributor for the Products of whatever nature must receive the prior approvals of the Principal which reserves the right to veto the same entirely at its discretion.

7.4 The cost of all merchandising returns from customers relating to the Products shall (unless otherwise agreed in writing or in respect of Products which the Principal is obliged to replace as defective in accordance with its warranty obligations under Schedule 5) be borne by the Distributor.

8 Sales and marketing policies

8.1 The Distributor shall conform to the general sales and marketing policies philosophies and principles of the Principal and the Principal reserves the right to issue directions from time to time to the Distributor to ensure such conformity.

8.2 Selling prices for the sale of the Products by the Distributor shall be established and revised from time to time by the Distributor.

8.3 The Distributor undertakes not to alter treat or otherwise deal with any of the Products (or their packaging) or to present any such Products for sale in a group package without in both cases obtaining the prior written consent of the Principal.

9 Monthly reports

9.1 The Distributor shall send to the Principal by the thirtieth day following the end of each calendar month during the continuance of this Agreement a report of sales made of the Products during that month together with such other marketing and other information in relation to the operation of the Agreement as the Principal may reasonably require. Forms for these reports will be supplied by the Principal.

10 Intellectual property rights

10.1 It is agreed that all rights to the Trademark (and all other intellectual property rights relating to or subsisting in the Products) are and shall remain the exclusive property of the Principal. The Distributor shall at the expense of the Principal enter into such agreements with the Principal and shall execute such documents and carry out such actions as may be necessary to protect such rights of the Principal.

10.2 The Trademark shall not be used in any manner liable to invalidate the registration thereof and the right to use the Trademark in connection with the appropriate Products is only granted to the extent that the Principal is able to do so without endangering the validity of the registration.

10.3 The Distributor shall (in so far as it becomes aware thereof) notify the Principal of any unauthorised use of the Trademark. At the request and cost of the Principal the Distributor shall take part in or give assistance in respect of any legal proceedings and execute any documents and do any things reasonably necessary to protect the Trademark.

11 No joint venture or partnership

11.1 Nothing in this Agreement shall create a partnership or joint venture between the parties hereto and save as expressly provided in this Agreement neither party shall enter into or have authority to enter into any engagement or make any representation or warranty on behalf of or pledge the credit of or otherwise bind or oblige the other party hereto.

12 Commencement and term of agreement

12.1 This Agreement shall commence on [the date of signature hereof] (the "Effective Date") and shall continue unless and until terminated in accordance with cl 12 or 13.

12.2 The Principal may terminate this Agreement at any time by not less than [12] months' notice provided that at the same time the Principal serves notice of the same length upon all its Authorised Distributors and Authorised Retailers for the Products in order to terminate all Authorised Distributor Agreements and all Authorised Retailer Agreements with the intention of disbanding and terminating the activities of its selective distribution network for the Products.

12.3 The Distributor may terminate this Agreement at any time by six months' notice to the Principal.

12.4 The Distributor shall obtain at its own expense all necessary permissions consents and licences (including but without limitation those required to be given by any government department or any body constituted for licensing or other regulatory purposes relating to the products) to enable the Distributor to market distribute and sell the Products and to ensure the full and legal operation of this Agreement. [For the avoidance of doubt, all taxes, charges, levies and fees of any kind imposed on the import or purchase of the Products shall be for the account of the Distributor.]

12.5 If the said permissions consents and licences are not obtained and fully operative within a period of [six] months from the Effective Date the Principal shall thereafter have the option to terminate this Agreement immediately by notice to the Distributor. The said option shall cease if (prior to its exercise) the aforesaid permissions consents and licences have in fact been obtained and are fully operative even though this has been achieved outside the said period of [six] months.

12.6 The Distributor shall not be entitled to any compensation on the termination of this Agreement under cl 12 or 13 for any cause whatsoever.

13 Summary termination

13.1 Without prejudice to any right or remedy the Principal may have against the Distributor for breach or non-performance of this Agreement the Principal shall (subject to cll 13.4 and 13.5) have the right summarily to terminate this Agreement:

13.1.1 On the Distributor committing a material breach of this Agreement providing the Distributor has been advised in writing of the breach and has not rectified it within 21 days of receipt of such advice.

13.1.2 If the Distributor shall have any distress or execution levied upon its goods or effects.

13.1.3 On the commencement of the winding up or bankruptcy of the Distributor or on the appointment of a receiver or administrator of the distributor's assets or on the Distributor ceasing to do business at any time for thirty consecutive days (other than for annual holidays).

13.1.4 On the Distributor for any reason of whatsoever nature being substantially prevented from performing or becoming unable to perform its obligations hereunder.

13.1.5 On the Distributor assigning or attempting to assign this Agreement without the prior written consent of the Principal.

13.1.6 If control of the Distributor shall pass from the present shareholders or owners or controllers to a competitor of the Principal in respect of the Products.

13.2 On the Distributor ceasing to comply with any of the Distributor Requirements provided that (where the relevant breach is remediable) the Principal shall have given to the Distributor notice of such failure and the Distributor shall have failed to remedy the breach complained of within [30] days of the receipt of such notice.

13.3 On the Distributor committing any breach or failing to comply with any legislation prohibiting or regulating unfair trading practices which may from time to time be in force in any area in which the Distributor sells the Products provided that the Principal shall have served notice requiring the Distributor to cease such practice and the Distributor shall have failed to do so within [30] days of receipt of such notice.

13.4 If the Distributor contends that termination has been effected under cl 13.2 in bad faith or that the Distributor has not in fact ceased to comply with the relevant Distributor Requirement as alleged the Distributor shall have the right to appeal against the termination of this Agreement by submitting the matter for resolution by an arbitrator in accordance with cl 19. In the event of such an appeal the notice shall be suspended pending its outcome and immediately upon the giving of the decision by the arbitrator the notice shall thereupon be cancelled or have immediate effect depending upon whether the appeal is allowed or disallowed respectively.

13.5 No termination shall take effect under cl 13.3 if the Distributor contests the same unless, and until a court of competent jurisdiction rules (upon the application of the Principal or otherwise) that the Distributor has in fact carried on the unfair trading practice in question and upon the giving of a ruling to this effect this Agreement shall thereupon automatically terminate.

14 Effect of termination

14.1 Upon termination of this Agreement from any cause whatsoever pursuant to cl 12 or 13 the Distributor shall at the request of the Principal promptly return to the Principal all documentation of any nature whatsoever in his possession or control relating to the Products or to the Principal and to the activities of the Distributor in relation to the Products or the Principal (other than correspondence between the Distributor and the Principal which does not relate to technical matters).

14.2 Upon such termination the Distributor shall cease to describe or refer to itself in any way as an Authorised Distributor for the Products, shall have no further rights to use the Trademark in any way whatsoever and in particular but without prejudice to the generality of the foregoing shall cease to use the Trademark on its letterheads packaging vehicle liveries or elsewhere and shall at the request of the Principal sell any stocks of the Products remaining in its ownership at the date of termination in packaging which bears neither the Trademark nor the name of the Principal.

14.3 Upon such termination the Distributor shall (if so required) supply the Principal with a list of the Distributor's customers for the Products.

14.4 Upon such termination the Distributor shall (if legally possible) assign to the Principal free of charge all permissions consents and licences (if any) relating to the marketing and or distribution and or sale of the Products and execute all documents and do all things necessary to ensure that the Principal shall enjoy the benefit of the said permissions consents and licences after the said termination to the entire exclusion of the Distributor.

15 Confidentiality

15.1 The Distributor shall keep strictly confidential not disclose to any third party and use only for the purposes of this Agreement all information relating to the Products (whether technical or practicable) by way of a secret ballot and to make proper arrangements for accurately counting the votes. In practice, where the elections concerned require a large number of votes (often from different sites), it is best practice to require an independent, specialist organisation to carry out the election procedures. No employee affected by the transfer may be "unreasonably excluded from standing for election" and all affected employees must have the right to vote.

Finally, in the event that:

> "after the employer has invited any affected employees to elect representatives, they fail to do so within a reasonable time, he shall give to each affected employee the information set out in Regulation 13(2)"

otherwise required to be given to the elected representatives pursuant to the Regulations. However, it appears that, having done this, there is then no further obligation upon the employer to consult directly with all of the affected employees, although good industrial relations would suggest that the offer to hold at least some direct meetings should be made.

Complaints of failure to comply with the Regulations can be made by any of the affected employees to an employment tribunal. However, where the claim relates directly to an employee or trade union representative (for instance, victimisation by the employer, or refusal to allow time off to perform the required duties), the person concerned must apply directly. In practice a complaint is often made on behalf of all affected employees together, usually by a trade union. Technically this is not a class action, but a number of separate actions, one for each affected employee, which are normally consolidated by the tribunal and heard as one, since the facts are the same in each case. Apart from complaints of a failure to consult at all, the two most common complaints are that employee representatives already elected for some other purpose did not have the appropriate authority to consult on behalf of their electorate about the transfer (in this case the employer has the burden of proving that they were in fact so authorised) or that insufficient information for meaningful consultation has been provided, which also, in a sense, amounts to a complaint that there has been no proper consultation. (See for instance *Lancaster University v University and College Union* (Employment Appeal Tribunal) [2011] I.R.L.R 4, a case on consultation in relation to redundancy (where the same rules on consultation apply) in which it was held that merely sending a list of affected employees to the trade union concerned did not amount to an effective consultation.)

If the tribunal finds that a failure has occurred, it has power to impose a protective award of up to 13 weeks' wages in respect of each employee affected by that failure. Liability is joint and several on the transferor and transferee. In *Sweetin v Coral Racing* [2006] I.R.L.R. 252 and *Zaman v Kozee Sleep Products Ltd (t/a Dorlux Beds UK)* [2011] I.C.R. D5, the Employment Appeal Tribunal reiterated the Court of Appeal's decision in *Susie Radin Ltd v GMB* [2004] 2 All E.R. 279 that the purpose of the protective award is to provide a sanction for the employer's breach rather than simply to compensate. Where there has been no consultation at all it will be appropriate for the tribunal to start with the maximum—13 weeks' pay—award and then establish if there are any mitigating circumstances to justify less than the maximum. Clearly if a "collective" action has been brought on behalf of all employees affected by the transfer, the

sums concerned could be significant. This award cannot, however, prevent the transfer taking place.

Finally, *Royal Mail Group Ltd v Communication Workers Union* [2009] EWCA Civ 1045 provides useful authority on the standard of care to be taken by the employer when compiling the information to be provided to the employee representatives. It must be complete enough to form the basis for meaningful consultation, but there is no obligation on an employer to warrant the accuracy of information it gives and a genuine, albeit mistaken, belief on the part of the employer that the information provided is correct is sufficient. A particular problem for employers is balancing the statutory obligation to inform and consult with obligations of confidentiality. Whilst reg.15(2) puts forward the opportunity for an employer to argue in defence to a claim for a protective award that he failed to inform and consult owing to the existence of special circumstances, it would be unwise to rely on this defence. Essentially, a trade off has to be reached between the cost of releasing the information and the costs of potential protective awards.

Finally, it should be emphasised that the transfer of undertaking position in other countries in the EU is not necessarily the same as that described above. Although the original Directive was a harmonisation measure, local employment law in other Member States (particularly France, Germany, Belgium and Holland) applies more stringent requirements as to consultation, in particular, in some cases, the need to actually reach agreement with the affected employees before the transfer can take place.

The application of the Regulations

11–7.3 It should be noted that whether or not the Regulations apply to a transaction is a question of fact to be determined by the appropriate tribunal (which may include the European Court of Justice), and that neither the parties to the transfer nor the employees concerned can contract out of their rights and duties under the Regulations.

In considering the authorities it is important to realise that from the very start of the Regime under the Acquired Rights Directive there was a tension between those who wished to apply the Directive narrowly and those who wished to apply it more broadly to cover what in the UK since 2006 would be regarded as a service provision change caught under reg.3(1)(b) of the 2006 Regulations as discussed in Chapter 11–7.1 above.

Clearly, a transaction whereby a business is expressed to be transferred as a going concern, together with goodwill, and the right for the purchaser to describe himself as carrying on the business as a successor to the seller, will be a business transfer (see *Premier Motors (Medway) Ltd v Total Oil (Great Britain) Ltd* [1984] I.C.R. 58 EAT; and *Spijkers v Gebroeders Benedik Abattoir CV* [1986] 2 C.M.L.R. 296 ECJ) while the sale of a few assets and contracts will be an asset sale (see *Gibson v Motortune Ltd* [1990] I.C.R. 740 EAT) not subject to the Regulations. However, there are many variations between these two extremes where the distinction becomes blurred.

According to *Watson Rask & Christensen v ISS Kantineservice A/S* [1993] I.R.L.R. 133 ECJ, the main question to be determined is whether there is a transfer of a "business activity" as a going concern, and that this can best be decided by looking at the type of undertaking, what assets and liabilities were being transferred, whether employees and/or customers were being taken on by the new owner, and the degree of similarity between activities before and after the transfer. However, the fact that no tangible property has been transferred as part of the transaction is not by itself fatal to the application of the Directive, and, hence, in the UK, the Regulations.

The lack of emphasis upon transfer of property increased in subsequent ECJ decisions, and it was affirmed that the Directive applied both where an outsourced activity was taken back in-house (*Francisco Hernandez Vidal SA v Perez* (C127/96) [1999] I.R.L.R. 132) and where, on the expiry of an outsourcing contract, a new concern took over the outsourced activity (*Sanchez Hidalgo v Asociacion de Servicios Aser* (C173/96) [1998] E.C.R. I–8237). In the ECJ case *Christel Schmidt* [1994] 1 E.C.R. I–1311, the court held that a transfer of undertaking could take place even if there was no transfer of assets or other physical materials between the transferor and the transferee. Finally, in *Merckx v Ford Motors Co Belgium SA* [1996] I.R.L.R. 467, the ECJ held that a transfer of undertaking can take place even when there is no contract between the transferee and the transferor.

The European Commission was not happy with this situation and attempted to amend the Acquired Rights Directive, to make it clear that transfers of the kind in *Christel Schmidt* should be outside the Directive, but the European Parliament would not accept the amendment. In *Ayse Suzen v Zehnacker Gebaudereinigung GmbH Krankenhausservice* [1997] I.R.L.R. 255, the ECJ clarified the situation by holding that (in a situation very similar to *Christel Schmidt*) there was no transfer of an undertaking. The court said that an entity could not be reduced to the activity entrusted to it, and that the mere loss of a service contract to a competitor cannot by itself indicate the existence of a transfer within the meaning of the Directive. The court went on to say that every case depended upon its own facts and that the correct test for whether there had been a transfer of undertaking was set out in *Spijkers*.

Decisions in the UK prior to *Ayse Suzen* were undecided as to how flexibly to apply the then version of the current Regulations and in some cases applied it to situations which were clearly no more than what would in the 2006 Regulations be classed as service change provisions. For instance in *Dines v Initial Healthcare Services Ltd* [1994] I.R.L.R. 336, there was held to have been a transfer of undertaking where a hospital ceased to use one cleaning contractor and arranged for a new one to take over the cleaning of the hospital under a new contract. Following the decision in *Ayse Suzen* this was clearly bad law.

In looking at the subsequent authorities decided in the UK after *Ayse Suzen* but before the service provision change was brought in under art.3(1)(b) of the 2006 Regulation, the only issue to be considered was whether there had been a transfer of an economic entity and it must be remembered that, although some of the situations considered were held not to be transfers of undertakings, they might well in fact have amounted to a service provision change if art.3(1)(b) had then been in force.

The Court of Appeal considered the current state of affairs after *Suzen* so far as the UK is concerned in two cases, which applied the same principles but came to opposite conclusions.

In *Betts v (1) Brintel Helicopters Ltd (2) KLM ERA Helicopters (UK) Ltd* [1997] 2 All E.R. 840, Brintel had a contract to provide helicopter services, but later part of the contract was awarded to KLM, who moved its operations from Beccles to Norwich, but did not take over staff or equipment from Brintel. KLM argued, relying on *Suzen*, that the fact that an activity which had been contracted to Brintel had now been contracted to KLM was not by itself enough to effect a transfer of undertakings. In general an

undertaking would also consist of property, staff and other assets, and as KLM had not purchased assets from Brintel or employed any of its staff, the Regulations did not apply. The Court of Appeal agreed, holding that it was necessary to determine whether the operation at Beccles had been an undertaking or part of an undertaking and if so, whether the undertaking was transferred so that it retained its identity in KLM's hands. Applying *Suzen*, the Beccles operation was an undertaking which consisted of assets which included not only staff, but also infrastructure, buildings and contracts, but as the vast majority of Brintel's assets had been retained by it, there was no transfer of the undertaking so that it could be said to have retained its identity with KLM.

In *ECM (Vehicle Delivery Services) Ltd v Cox* [1999] 4 All E.R. 669, there was a vehicle delivery contract under which the contractor delivered VAG cars from Grimsby docks to VAG dealers throughout the UK, using 23 drivers who spent about 50 per cent of their time working on the contract. The contract was lost to ECM, who did not take on any of the drivers who had worked on the VAG contract. The drivers applied to an industrial tribunal which held that the VAG contract and the associated activities constituted a "discrete economic entity", that the contract had been transferred to ECM and that the economic entity retained its essential character following the transfer, despite certain differences. ECM's appeal to the EAT was dismissed, and it appealed to the Court of Appeal, relying on *Suzen* for the contention that where the only continuing activity following a transfer was the service itself, there could be no finding that an undertaking had been transferred. The Court of Appeal dismissed the appeal, holding that the test had been correctly applied by the tribunal. In particular, the tribunal had been entitled to conclude that while there were differences between the manner of operation of the VAG contract, the customers were essentially the same and the work being performed was the same, in that cars were still unloaded on the Grimsby docks, put onto transporters and driven to VAG dealers. The finding of those facts justified the ruling by the tribunal that there had been a transfer of an undertaking. There was no rule of law that in cases where a service contract had been lost to a rival and no staff had been taken on there could never be a transfer of an undertaking. The issue had to be determined by reference to all the facts and circumstances of the particular case, having regard to the legal criteria set down by the ECJ in *Spijkers*.

There have also been two decisions in the Employment Appeal Tribunal, which have applied the same principles and come to much the same conclusion as the Court of Appeal in *ECM*.

In *Cheesman v R Brewer Contracts Ltd* [2001] I.R.L.R. 144, the EAT again confirmed that the fact that none of the previous contractor's employees had been engaged by the new contractor was not determinative of the question whether there had been a relevant transfer. The tribunal was required to take all facts surrounding a transfer into account and to ensure that none of those facts was considered in isolation. The correct approach was to ask whether there had existed an economic entity within the meaning of the Regulations, and then whether, if there had been such an entity, there had been a relevant transfer.

In *Lowe v Dudley Bower Building Services Ltd* [2003] I.C.R. 843, EAT, Lowe's employer had a contract to perform electrical work for the RAF. This work was carried out by Lowe. His employer lost the contract, upon a retender, and the new contractor refused to employ Lowe. The court held that Lowe and the activity that he carried on was a stable economic entity which had been transferred. The existence of assets was not a requirement in sectors which depended on manpower. The court accepted the principle in *Suzen* that an entity could not be reduced to the activity entrusted to it, but stated it was required to apply the usual tests as to the existence of a stable economic entity. Here factors such as workforce, management staff, organisation of work, operating methods and operational resources were relevant. The application of those circumstances was a question of fact and degree. There was no requirement that there had to be more than one employee.

Following the creation of the new rights under the service provision change legislation in reg.3(1)(b) of the 2006 Regulation, the distinction between three possible situations has become clear. These are (i) transfer of undertaking with or without an associated service provision change (ii) some transfer of assets and contracts which is not a transfer of undertaking and does not amount to a service provision change and (iii) a service provision change which is not associated with a transfer of undertaking.

So far as EU law is concerned it is quite clear the position in *Ayse Suzen* still holds good and that the Acquired Rights Directive (and hence art.3(1)(a) of the 2006 Regulation) does not apply to a service provision change. In *CLECE SA v Martin Valor* (C–463/) [2011] 2 C.M.L.R. 30 the ECJ applied and confirmed the principle in *Ayse Suzen* when it held that the Acquired Rights Directive did not apply to a situation in which a municipal authority which had contracted out the cleaning of its premises to a private company decided to terminate its contract with that company and to undertake the cleaning of those premises itself by hiring new staff for that purpose. This would of course have been a service change provision under reg.3(1)(b) of the 2006 Regulation.

In situations (i) and (ii) above, where the situation does not involve any service provision change, the English Courts continue to follow the decision in *Ayse Suzen*. In the case of situation (i) where there is a clear and straightforward transfer of an economic entity the fact there is or is not a service provision change associated with it is in fact irrelevant, since if reg.3(1)(a) clearly applies there is not need to go on to consider the applicability of reg.3(1)(b).

In *Millam v The Print Factory (London) 1991 Ltd* [2007] I.C.R. 1331, the Court of Appeal held that a subsidiary's employees may transfer to a holding company following a share sale, where the business activities of that subsidiary are integrated into the holding company's business to such a degree that the business entity itself is found to have transferred into the hands of the holding company. This decision has potentially serious ramifications for group reorganisations and share sales, although the precise scope of the decision remains untested.

In *Law Society of England and Wales v Secretary of State for Justice* [2010] EWHC 352 (QB) the Court held that there was no transfer of the undertakings of the Law Society's Legal Complaints Service to the Office for Legal Complaints, set up under the Legal Services Act 2007, as there was no transfer of an economic entity which retained its identity.

In *Nottinghamshire Healthcare NHS Trust v Hamshaw* [2011] WL 2747652, the Employment Appeal Tribunal held that an employment judge had been entitled to find that there had been no relevant transfer of undertaking where the residents of an NHS care home were rehoused in individual homes following the closure of the home and the care workers formally employed by the NHS trust were employed by different care providers to provide support to the residents. The Tribunal stated that whether or not a relevant transfer had occurred was a highly fact-sensitive judgment. Describing the

economic entity as the home was convenient shorthand for the entity of the home, its premises, staff, residents, equipment, resources and organisation. The care assistants and residents transferred but the premises, equipment, resources and organisation did not. The employment judge had been entitled to find that the service after transfer was "fundamentally different" from that which had operated at the home and that there had therefore been no relevant transfer.

So far as situation (iii) above is concerned, the Court of Appeal has laid down important guidelines on the application of reg.3(1)(b) where there is no question of a concomitant transfer of undertaking under reg.3(1)(a). In *Hunter v McCarrick* [2012] EWCA Civ 1399 the appellant employee appealed against a decision that the transfer of his employment to the respondent individual did not amount to a service provision change within reg.3(1)(b). McCarrick managed a property portfolio owned by a company of which Hunter was the managing director. Hunter sold his company, including the property portfolio, but the sale did not formally proceed. Nevertheless, it was agreed in February 2009 that some employees, including McCarrick, would still transfer to the new company (WCP). He therefore continued to manage the property portfolio, but was paid by WCP instead of by Hunter's company. In August 2009, WCP ceased to perform the property management services because receivers appointed by the mortgagee of Hunter's company assumed control of the properties. The receivers appointed a new property management company. However, Hunter paid McCarrick out of his own pocket to assist the new company in the portfolio management. The employment tribunal considered that both the February and the August transfers constituted service provision changes within reg.3(1)(b). The Employment Appeal Tribunal disagreed, holding that, on a straightforward and common sense application of the statutory language, the August transfer could not be a service provision change because the portfolio activities before and after the transfer were not carried out for the same client. McCarrick submitted that, although, read literally, reg.3(1)(b) envisaged that the same service would be provided to the same client throughout, its clear purpose was to protect employees, and that objective could not be achieved unless a wider interpretation of the provision was adopted.

The Court of Appeal dismissed the appeal, and held that there was no room for a purposive construction with respect to the scope of reg.3(1)(b). The provision gave protection beyond that circumscribed by EU law and was therefore not subject to the requirement for a purposive interpretation. Rather, a natural construction gave effect to the draftsman's purpose. The concept of a change of service provision was not complex and the ordinary language of reg.3(1)(b) accurately defined the range of situations that it was intended to protect. There was no basis on which to give a broader or expanded meaning,

Liabilities transferred under the Regulations

11–7.4 Under the Regulations the basic principal of transfer of liabilities is set out as follows in reg.4(1):

"a relevant transfer shall not operate so as to terminate the contract of employment of any person employed by the transferor and assigned to the organised grouping defendant from benefiting (or continuing to benefit) from the past misuse. Whether this is a sound basis for granting an injunction I shall consider below."

Arnold J. then goes on to consider the basis on which an injunction preventing past misuse could be granted. After an examination of the authorities he concludes:

"i) In general, the remedy for past misuse of confidential information is a financial one. Where appropriate, the claimant can claim a restitutionary remedy, namely an account of profits, which deprives the defendant of the benefit of his wrongdoing.

ii) As the law presently stands, it is not clear whether an injunction can be granted to prevent a defendant from benefiting from a past misuse of confidential information. Laddie J in Ocular Sciences interpreted Lord Goff in Spycatcher as having concluded that the answer was no, but I am less confident of this . . .

iii) . . . . When an interim injunction is sought, the court's task is to hold the ring pending trial. It is not in a position to determine the parties' legal rights or to award either compensatory or restitutionary remedies. In these circumstances a limited injunction to prevent the defendant from benefiting from his (alleged) past misuse of confidential information may be the best way to preserve the status quo pending trial. If it turns out to have been wrongly granted, the court can require the claimant to compensate the defendant under the cross-undertaking in damages.

iv) In any event, it seems to me that . . . considerable caution is required both as to whether to grant such an injunction at all and, if so, as to its form and duration . . . the duration of any such injunction should not extend beyond the period for which the defendant's illegitimate advantage may be expected to continue."

Finally Arnold J. considers the issue of misuse of confidential information in relation to what he calls "derivative products". He takes the term and its definition from the judgment of Laddie J. in *Ocular Sciences* which is as follows:

"where the defendant's derivative products, process or business have been made from or with the assistance of information which is still confidential but where they do not themselves directly disclose or incorporate the information. If the derivative products or process are regarded merely as illicit benefits flowing from misuse of confidential information, then, for the reasons set out above, I do not think that is a basis which would justify the court in granting an injunction. On the other hand it may be possible to argue that the continued use or exploitation of the derived product is to be regarded as a continued use or exploitation of the confidential information which was utilised for their creation."

It could well be argued that the misuse of confidential information in relation to derivative products is just another instance of the past misuse of confidential information as a springboard. The only issue here is that unlike the situation that Arnold J. considered above, the information concerned has not ceased to be confidential, so there is no issue

of public domain which would, in theory, prevent the granting of an injunction because the information has ceased to be confidential. Arnold J. analysed Laddie J.'s judgment and came to the following conclusions:

"Laddie J's reasoning may be summarised as follows:

i) The purpose of an injunction to restrain disclosure or use of confidential information is to prevent further disclosure or use of the confidential information in the future.

ii) Where a product embodies or discloses confidential information, or is manufactured using confidential information, then an injunction to restrain use of the confidential information will automatically restrain the continued manufacture and sale of the product.

iii) An injunction may also be granted to restrain the manufacture or sale of a derived product where the manufacture of it represents a continued use of the information having regard to the extent and importance of the use of the information.

iv) Otherwise, the appropriate remedy in respect of the manufacture and sale of products derived from a past misuse of confidential information is a financial one.

Laddie J's analysis of this question is premised on his previous conclusion that no injunction should be granted purely to prevent a defendant from benefiting from a past misuse of confidential information. For the reasons I have explained, I am less confident that that premise correctly states the law, but I do agree that, at the very least, the court must be cautious in granting such an injunction lest it put the claimant in a better position than if there had been no misuse. If a permanent injunction is granted to restrain the manufacture and sale of a product which is derived from a past misuse of confidential information, but such acts do not amount to a continued misuse of the information, then the risk that the claimant will end up in a better position than if there had been no misuse may become acute. In general, therefore, I consider that Laddie J's analysis represents the correct approach."

The most recent case to discuss the springboard doctrine and to consider the question of the remedy of damages in order to compensate for the head start obtained by the past misuse of confidential information as opposed to an injunction (even if only for a limited time) is the Court of Appeal decision in *Force India Formula One Team Ltd v 1 Malaysia Racing Team Sdn Bhd* [2013] EWCA Civ 780, although the word "spring board" is not mentioned in the decision.

At first instance, the judge found that the consultant employed by Force India to design its racing car had not copied or taken the aerodynamic system of this car, when subsequently working on a similar racing car for 1 Malaysia. However, he found that the consultant had made use of confidential information relating to the design of Force India's car, in order to save time in producing a model of the new car that could be subjected to wind tunnel testing. The judge then decided that 1 Malaysia should compensate Force India for the benefit of the head start it had gained from the consultant's misuse of Force India's confidential information by the payment of damages, the quantum to be assessed by reference to the cost of engaging a consultant to do the work saved. The Court of Appeal agreed with the judge that this was an appropriate measure of compensation for misuse of confidential information. Lewison L.J. commented on and quoted the decision in *Seager v Copydex* with approval and stated as follows:

> "In my judgment it is clear from these cases that, depending on the facts, the cost of engaging a consultant can be an appropriate measure of compensation for misuse of confidential information if that is an alternative means of obtaining an equivalent benefit from another source . . . In selecting as the measure of damages the cost of employing a consultant in order to obtain an equivalent benefit from an alternative source the judge was, in my judgment, following a well-trodden path. I see no error of principle here. ."

Going on the above analysis, it is now possible to lay down some tentative rules in relation to remedies for misuse of technical information.

The first is that both interim and final injunctions are (subject to the exceptions in *Shelfer*) likely to be granted to prevent continuing misuse of confidential information.

The second is that in most cases where there has been a past misuse of confidential information, which has subsequently ceased to be confidential, the correct remedy is normally damages or an account of profits. One possible exception to this is the grant of an interim injunction to preserve the status quo pending trial on the merits.

The third is that where the technical information has been used as a "springboard" or in the production of a derivative product and that misuse is a continuing one, then the grant of a final injunction is possible provided the information remains confidential (see for instance *Peter Pan*).

The fourth is that where there has been a past misuse of confidential information as a "springboard" or in connection with a derivative product, it is possible but unlikely that, if the information remains confidential, an interim or even a final injunction might be granted, perhaps to restrain further disclosure. However, even in this case, and certainly if the information has ceased to be confidential, damages or an account of profits is more likely to be the appropriate remedy.

The fifth is that it is easier for the court to classify the use of information as a springboard, rather than copying, where the plaintiff has not himself put a product on the market utilising the relevant information. In borderline cases, the existence of two rival products can tip the balance towards a finding of "copying".

The sixth is that evidence of fraud, or serious breach of duty, will incline the court to grant a final injunction rather than damages whether or not dealing with a "springboard" case. Given that "equity acts on the conscience" and that an injunction is a discretionary remedy, it is quite clear that the decisive factor in many of the cases has been the degree of disapproval which the court held for the activities of the defendant. (See the comments to this effect on *Shelfer*) This would also go towards an explanation of why a final injunction was granted in *Peter Pan, Terrapin* and *Cranleigh*. As can be seen in Arnold J.'s judgment in *Vestergaard*, he, too, was not convinced that it was impossible to grant a final injunction to prevent continuing misuse of information which was no longer confidential.

However, despite the detail of the analysis and commentary above and the effort expended on deciding into which category each case falls, it should never be forgotten that the grant of an injunction is an equitable remedy to be granted or withheld by the trial judge as he thinks best in all the circumstances of the particular case.

Express documentation

13–8 Given the far-reaching nature of the equitable principles relating to confidentiality, it may well be asked why any express documentation is necessary at all. There are, however, a number of good reasons for providing express documentation in commercial transactions.

Express documentation can take the form of either a confidentiality undertaking or a confidentiality agreement.

An undertaking is not a contract, and therefore need not be supported by consideration. Its purpose is to provide evidence as to what information the recipient has received, the purpose for which he has received it, and to show that it was communicated to the recipient in confidence. The undertaking thus provides the necessary evidence to trigger the operation of the general principles of equity protecting confidential information, but does not of itself offer any protection.

Where a confidentiality agreement is used, the situation is somewhat different. The first question is whether the protection afforded to the information covered by the agreement arises solely under contract, so that the protection in equity is displaced by the express terms of the contract, or whether the equitable protection subsists in addition to the contractual protection. In the view of Megarry J. in *Coco v AN Clark (Engineers) Ltd*, above,

> "the obligation of confidence may exist where, as in this case, there is no contractual relationship between the parties. In cases of contract, the primary question is no doubt that of construing the contract and any terms implied in it."

Where the express terms of the contract cut down on the protection which might otherwise be granted by equity, then it seems clear from the authorities, that to this extent the equitable principles are displaced. For instance, an obligation not to disclose confidential information for a fixed period of time will free the recipient from any obligation not to disclose once that period has expired, even if, in the absence of a contract, equity might have restrained him for longer (see *Potters-Ballotini Ltd v Weston-Baker*, above).

The real question to be asked, however, is can a confidentiality agreement impose, under contract, confidentiality obligations that are greater than those afforded under the general law? For instance, is it possible to restrain a recipient from using or disclosing confidential information after it has become common knowledge, because of publication by the donor or an unconnected third party—a situation where the general law would no longer impose a restraint? There is admittedly some doubt about this (see the comments of the Law Commission in their report on confidentiality mentioned earlier) but in general terms, in a commercial context, any imposition of confidentiality obligations of this nature could well be struck down as unjustifiable restraints of trade. On this point, reference should be made to the discussion above concerning the impact of doctrines of restraint of trade on the protection of confidential information in a commercial context. The dicta in *Yates Circuit Foil Co v Electrofoils Ltd* [1976] F.S.R. 345 at

384, mentioned in that section, would equally apply to express contracts, as would the judgment in *Faccenda Chicken Ltd v Fowler*, above.

A similar question that can be asked is whether a confidentiality agreement could bind the recipient in regard to information which would be (at least arguably) of too trivial a nature to be subject to the general equitable protection afforded to secret information as described in *Saltman Engineering Co Ltd v Campbell Engineering Co Ltd*, above.

Although such matters are not free from doubt, it is normally better not to produce general commercial confidentiality agreements that impose obligations greater than those which could be enforced under the general equitable principles. Such a course is not only likely to cause problems of restraint of trade, but it is also likely to raise commercial difficulties with the other party. Furthermore, it has to be asked whether there are any legitimate interests that are, in practical terms, really worth protecting, once one goes beyond the protection afforded by the general law.

The particular problems in relation to confidentiality clauses in employment contracts are discussed in detail in Ch.14. Know-how licences also cause considerable problems in this area, particularly under European competition law, and these issues are discussed in Ch.18.

Leaving aside questions of restraint of trade, the use of an agreement as opposed to an undertaking serves two clear purposes.

The first is to enable the parties to agree (in a legally enforceable document) a more circumscribed or clearly defined protection for confidential information than that afforded under the general law. Precise wording defining when information is to be regarded as common knowledge can solve the problems associated with the concepts of "public domain" and "publication", and the springboard doctrine discussed above. Further the parties can agree that no information shall be regarded as confidential after the expiry of a period of time, or that no protection will be granted to confidential information which is imparted orally. Such agreements are often more practical from a commercial point of view for both parties, who can define precisely what confidentiality obligations they wish to accept rather than relying on the broader and perhaps more imprecise doctrines of the general law.

The second is to impose upon a party (usually the recipient) legally enforceable obligations which are ancillary to the central obligations of confidentiality and not implied under the general law. An obligation to return documents containing confidential information upon demand, or the duty to maintain a system for recording the transmission and receipt of confidential information, can be imposed in this way. Another common instance is the imposition of an obligation to inform the donor if the recipient is requested to disclose confidential information to a court or to a government authority that has a legal right to require him to disclose it despite the obligations imposed on him. A contractual document is also useful in dealing with the issue of negligent or inadvertent disclosure. It has been said that the general law probably forbids both, but the situation is not entirely clear. Thus the best course is to insert express obligations on the recipient as to the procedures and level of care he must take to safeguard the confidential information and the documentation or other items in which it is embodied. Such obligations can also include a duty to enforce any duties of confidentiality owed to the recipient by his employees, insofar as this is necessary to prevent them disclosing the donor's information.

Freedom of information

13–9 A consideration of the scope of the Freedom of Information Act 2000 (the 2000 Act), which came fully into force on January 1, 2005, for public authorities is beyond the implications of this book. This section considers its implications for commercial undertakings.

The Act entitles any individual, company or other organisation to make a request to a public authority for information held by the authority and to be informed (subject to exceptions) within 20 working days whether the authority holds the information and, if so, to have the information communicated to them. The Information Commissioner is responsible for enforcing the 2000 Act and aggrieved applicants may appeal to him if they believe a public authority has failed to comply with an information request.

Public authorities include local and central government as well as, e.g. schools and colleges and the police.

Subject to exemptions, the Act applies to all information held by an authority, including information that may have been supplied by a commercial undertaking, e.g. information supplied as part of a tender for a local authority contract.

The two exemptions which are most likely to affect commercial undertakings are:

- information the disclosure of which would constitute an actionable breach of confidence. This is an *absolute* exemption (s.41);
- trade secrets or information the disclosure of which would be likely to prejudice a company's commercial interests (s.43). This is a qualified exemption, so that even if the exemption applies the public interest in withholding the information must still outweigh the public interest in disclosing it.

The public authority must decide for itself whether disclosure is in the public interest and each case will be determined on its own facts. Generally, the public interest is considered to be served when the disclosure of the information would do any of the following:

- further the understanding of, and participation in the debate of issues of the day;
- facilitate the accountability and transparency of the authority in relation to its decision making;
- allow individuals to understand decisions made by the authority affecting their lives and, in some cases, assist individuals to challenge those decisions;
- facilitate accountability and transparency in the spending of public money;
- bring to light information affecting public safety.

Clearly, commercial undertakings dealing with public authorities must emphasise what information they regard as confidential or commercially sensitive and the duration of confidentiality (e.g. indefinitely, until contract award, etc.)—typically this will be set out as an appendix to the contract—and that their contracts impose an obligation on the authority to consult them before disclosing sensitive or confidential information. It may have to seek an injunction if the authority persists with an intention to disclose, with which it disagrees. The 2000 Act can, of course, be used positively by commercial undertakings to obtain information about competitors.

Some case law is beginning to develop around the application of the exemptions. The leading case to date is *Derry City Council v Information Commissioner* (EA/2006/0014). The air carrier, Ryanair, had sent a fax marked "private and confidential" to the council setting out a number of terms for the operation of a scheduled flight service between Derry and London. The terms included details of its charges. The fax insisted on the planned service remaining confidential until publicly announced by Ryanair. A journalist submitted an information request for a copy of the fax. The council provided a redacted copy having removed some of the information regarding charges. The journalist believed that all of the information should have been disclosed. The Information Commissioner agreed and ordered full disclosure. The Information Tribunal dismissed the council's appeal.

The tribunal held that the council's commercial interests did not outweigh the public interest so the exemption in s.43 of the 2000 Act was not made out. More controversially, it denied that the exemption under s.41 applied. This was because s.41(1)(a) did not apply to information contained in a contract entered into by the authority with a third party—in other words it does not cover the commercial arrangements between a public authority and its contractual partners. Further, there could be no actionable breach of confidence as there would be a common law defence to such a claim based on the public interest in the disclosure of the information.

Decision Notice to Mid Suffolk District Council (Reference FS50131138, June 19, 2008) concerned a request under the Act for a copy of the tendering document submitted by the contractor chosen to carry out repairs and maintenance at a local leisure centre. The council refused to provide a complete copy on the grounds that the document contained financial information that was exempt under s.43. Specifically, the council argued that the information was exempt from disclosure as it would, or would be likely to, prejudice the commercial interests of the contractor. The Assistant Information Commissioner stated that there was no evidence that disclosure would prejudice either the contractor or the council and ordered disclosure. Since there was no prejudice likely to be suffered, it was not even necessary to apply the public-interest test under s.43. This decision clarified one effect of the *Derry* case, namely that although councils do not need to provide clear evidence that they have consulted with their contractor on the issue of disclosure and its effects, they must at least make convincing arguments that their representations have originated with the contractor.

Decision Notices relating to Brighton and Hove and East Sussex Councils (Reference: FER0073984 and FER0099394) was another decision to take a restricted view on the application of the commercial sensitivity exemption. The councils had entered into a waste management contract. Each council received an information request and disclosed certain parts of the contract but refused to disclose certain of the information on the grounds that it was commercially sensitive. (The application was actually made under the Environmental Information Regulations 2004 as well as the Act. The Regulations contain similar provisions to the Act, applicable to the environment, though there are differences, not the least of which is that there are no absolute exemptions under the

Regulations). The Information Commissioner took great care to spell out what information could and could not be disclosed. The former included all planning and development information other than systems planning and technical information; all pricing information other than highlighting specific costs and profits of the contractor; information on emissions and potential emissions; intended methods of dealing with by-products of the waste management process; all operational information. Information that could not be disclosed included specific information and technical information not otherwise in the public domain; the contractor's costs and profits; clawback of costs through the sale of by-products; and the contractor's quality operational manual. Clearly, this categorisation could change over time. This particular contract was a 25-year PFI contract and technical information, for example, could enter the public domain at a later stage during the lifetime of the contract.

Special considerations relating to commercial information

13–10 Finally, so far as protection of information in the commercial world is concerned, there are a number of specific issues which need to be considered.

First, in enforcing obligations of confidentiality the most important issues are evidentiary ones. Was there an obligation of confidentiality at all? If there was, to what information did it relate, and has the recipient actually misused or disclosed the relevant information? Express confidentiality undertakings or agreements should always be used (leaving the general principles of law as a backstop in case things go wrong) and, wherever possible, details of the information disclosed, and an acknowledgment of its receipt, should be part of the undertaking or agreement, or set out in subsequent documentation recording the transmission of information in reliance upon the undertaking or agreement. Failure to particularise the confidential information it is alleged has been disclosed or misused is one other frequent cause for failure to obtain relief in judicial proceedings. (See for instance *CMI Centres for Medical Innovation GmbH v Phytopharm Plc* [1999] F.S.R. 235 Ch D.)

Secondly, two areas where special care should be taken are pre-contract negotiations, where the parties often exchange confidential information without any formal protection, and the receipt of unsolicited inventions and advice. In the first case, the circumstances may be such as to give rise to an obligation of confidentiality, but it is still better to formalise the situation with proper confidentiality obligations. In the second case, the circumstances may again give rise to an obligation of confidence which, this time, in the case of the recipient, will be entirely unintended and unwelcome; here, it is best to avoid accepting unsolicited advice and inventions unless the offeror signs a waiver disclaiming his rights in respect of confidentiality over the information offered.

The dangers of informal disclosure were highlighted in *De Maudsley v Palumbo*, discussed above. Here the information, which was claimed to be confidential, was imparted orally while the plaintiff and defendant (two business acquaintances) were having supper on a social occasion. The court stated that, where there is no express declaration that the information is being disclosed in confidence, the test of whether the information was imparted in circumstances which by implication gave rise to a duty of confidence was an objective one. The issue was not what the parties' themselves thought about the situation, but what a reasonable third party would have thought under the