

ARE THEY WORTH THE EFFORT? – ACTION, INACTION AND ALL KINDS OF ENDEAVOURS IN A CONDITIONAL CONTRACT

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Edwin Johnson QC - Maitland Chambers

Edwin's practice is in property, chancery and commercial litigation and advisory work. His experience includes property disputes, professional negligence and general commercial and chancery work including trusts disputes, insolvency, development and other commercial contracts, building and construction work, insurance work and competition law. He was appointed Standing Counsel to the Rent Assessment Panel in 2000, was Chambers & Partners Real Estate Junior of the Year in 2005, was appointed Queen's Counsel in 2006, and was nominated for Chambers Bar Awards' Real Estate Silk of the Year in 2012 and 2013.

Edwin appears regularly in Courts and Tribunals at all levels. Edwin has never lost a case at the highest level: his most recent success has come in the Supreme Court in *Hosebay*. This followed consecutive successes in four House of Lords cases *Shalson*, *Boss Holdings*, *26 Cadogan Square* and *Atlantic Telecasters*.

Edwin's clients range from individuals to nation states and he has particular experience of acting for public authorities in relation to their property holdings, including the complex area of service charges in leases of public authority housing stock, rights of light, disputes over break clauses and conditional contracts/development contracts.

Recent cases of interest include *Kutchukian v Free Grammar School of John Lyon* [2013] (construction of break provisions), *Kim v Chasewood* [2013] (estoppel), *Morshead Mansions v Mactra Properties* [2013] (construction of service charge provisions), *Day v Hosebay* (whether properties are houses within the meaning of Section 2(1) of the Leasehold Reform Act 1967) and *Extra MSA v Accor* [2011] (whether conditional contract subject to implied term that party could not take advantage of own wrong).

MAITLAND CHAMBERS

7 Stone Buildings
Lincoln's Inn
London WC2A 3SZ

Tel: +44 (0)20 7406 1200

Email: ejohnson@maitlandchambers.com

Introduction

1. Hideous Developments Limited (“Hideous”) is looking for a major expansion of its residential housebuilding activities.
 - 1.1 Hideous thinks that it has found the perfect site when an agent effects an introduction to Green & Pleasant Land Bank Limited (“GP”). GP owns a large site (“the Site”), comprising picturesque agricultural land on the outskirts of a rural market town. Hideous decides that the Site is ideal for a substantial development of several hundred houses (“the Development”), on which it is confident that it will turn a substantial profit.
 - 1.2 There are two particular snags.
 - 1.3 First, the Site has no planning permission for residential development. Achieving this planning permission is not likely to be easy. Both Hideous and GP anticipate considerable local objection to the planning application, and considerable political pressure on the local planning authority to refuse the application.
 - 1.4 Second, the Site is subject to a restrictive covenant, dating from the 19th Century, which prevents residential use of the site. This covenant (“the Covenant”) was imposed by the Backward family, when the site was sold out of the Backward Estate in the 19th Century. There are question marks over whether the Covenant is still enforceable. GP has obtained an expensive Opinion from eminent Leading Counsel which, after much learned analysis and verbal teeth sucking, concludes that the better view is that the covenant is not enforceable against the Site. The Opinion acknowledges the possibility that the covenant would be found to be enforceable, if the matter came to be tested in Court. Leading Counsel is clearer in advising that, if the Covenant is enforceable, there is a good case for securing its discharge pursuant to Section 84 of the Law of Property Act 1925. Hideous is shown the Opinion by GP.

The Conditional Contract

2. Hideous is anxious to secure the Site. It has heard rumours that other housebuilders are circling. This is no time for caution. GP is however demanding a substantial sum of money for a site which may turn out not to be capable of development.

2.1 The solution is a conditional contract, entered into between the parties. Time is short and the conditional contract is drawn up in something of a hurry. The drafting leaves much to be desired.

2.2 The essential structure of the conditional contract (“the Contract”) is as follows.

- (1) Hideous agrees to purchase, and GP agrees to sell the Site, on the terms of the Contract.
- (2) The completion date will fall on the date on which the last of a number of specified conditions (“the Conditions”) is satisfied. Two of these Conditions are as follows.
 - (i) The obtaining of planning permission for the Development in a form specified in the Contract (“the Planning Permission”).
 - (ii) The securing of (a) the release of the Covenant by agreement, or (b) a decision of a Court that the Covenant is unenforceable against the Site, or (c) an order of the Upper Tribunal for the discharge of the Covenant.
- (3) Hideous agrees to use reasonable endeavours to obtain the Planning Permission including the making of an appeal against a refusal of the Planning Permission.
- (4) Hideous agrees to use best endeavours to secure (a) the release of the Covenant by agreement, or (b) a decision of a Court that the Covenant is unenforceable against the Site, or (c) an order of the Upper Tribunal for the discharge of the Covenant.
- (5) Satisfaction of the remaining Conditions is not expressed to be subject to a specific obligation on the part of Hideous of the kind set out (3) and (4)

above. Satisfaction of the remaining Conditions will however require action on the part of Hideous.

- (6) Both parties agree to use all reasonable endeavours to ensure that completion of the Contract takes place.
- (7) If all of the Conditions have not been satisfied by a specified date ("the Specified Date") each party has the right to terminate the Contract by giving notice in writing. In the case of Hideous this right of termination is available, as from the Specified Date, save where Hideous has breached its obligation to use all reasonable endeavours to ensure that completion of the Contract takes place.

2.3 The purchase price, payable on completion, is £10 million. At the time of entry into the Contract, Hideous estimates that the profit it should be able to realize on the Development is some £3 million. This figure takes into account the anticipated costs to Hideous of obtaining the Planning Permission (including running an appeal) and dealing with the Covenant. In the pre-Contract negotiations over the price the parties exchange rival valuations of the likely profit to be realized from the Development, which have been prepared on the same basis as the estimate made by Hideous.

Events

3. Following entry into the Contract, Hideous sets about the tasks of securing the required planning permission and dealing the Covenant.
 - 3.1 As anticipated, the application for planning permission ("the Application") runs into considerable local opposition. Bowing to local pressure the local authority refuses the Application, whereupon Hideous launches an appeal ("the Appeal"). Hideous decides to take advice on the prospects of success for the Appeal. The advice received by Hideous, which is shared with GP, is that the Appeal has good prospects of success.

- 3.2 A point which becomes apparent in the planning process is that, if the Application is to be permitted at all, a much larger Section 106 contribution will be required than Hideous had anticipated when it entered into the Contract. In financial terms, the increase in the Section 106 contribution is likely to amount to an additional £100,000, over and above the originally estimated cost of £250,000.
- 3.3 In relation to the Covenant, a letter arrives from the Backward family's solicitors, shortly after the Application is made, asserting that the Covenant prevents residential development of the Site, and that Hideous will find itself on the wrong end of a claim for injunctive relief if it proceeds with the Development. Hideous replies, by its solicitors, asserting that the Covenant is not enforceable and that, even if the Covenant is enforceable it can easily be removed by an application for discharge of the Covenant pursuant to Section 84 of the Law of Property Act 1925. Hideous says that it will see the Backward family in Court or the Upper Tribunal or both, if the Backward family does not accept that the Covenant is unenforceable.
- 3.4 A lengthy chain of correspondence ensues. At the end of this chain of correspondence, when matters have reached the stage of Hideous sending a formal letter of claim, a letter arrives from the Backward family's solicitors, headed without prejudice, offering a release of the Covenant in exchange for a payment of £200,000.

Disaster

4. Considerable time has now passed, and the Development is looking distinctly unattractive. The residential development market is recovering from the crash, but not yet to the point where the Development is financially attractive. The overseas bank, which was to have funded the Development, has collapsed amidst a welter of money laundering allegations. Hideous is doubtful that it will realize any profit from the Development.

Hideous seeks to exit the Contract

5. Looking for a way out of the Contract, Hideous decides to sit on its hands. The Appeal is not pursued. Hideous refuses to accept a higher Section 106 contribution. No action is taken in respect of the Covenant further to the letter of claim. The offer from the Backward family is allowed to expire without reply.
- 5.1 Hideous has the means to pursue the Appeal and to fund the more expensive Section 106 agreement which is likely to be part of the price of obtaining the Planning Permission. Hideous also has the means to pursue proceedings in respect of the Covenant or to pay what the Backward family is demanding for the release of the Covenant.
- 5.2 It is likely that vigorous pursuit of the Appeal would have secured the Planning Permission by the Specified Date. It is more uncertain that proceedings in respect of the Covenant, either in Court or in the Upper Tribunal, could have been concluded by the Specified Date. It is certain that acceptance of the Backward family offer would have resulted in an agreed release of the Covenant by the Specified Date. There would also have been time, prior to the Specified Date, for further negotiation with the Backward family.
- 5.3 None of the other Conditions were outstanding at the Specified Date.
- 5.4 Once the Specified Date has arrived, Hideous gives notice to GP to terminate the Contract.
- 5.5 So far as the Covenant is concerned, all of the above predates the decision of the Supreme Court in Lawrence v Coventry [2014] UKSC 13.

The dispute

6. GP refuses to accept the notice of termination. GP argues that Hideous is not entitled to terminate the Contract because, by doing so, Hideous is taking

advantage of its own wrongs; namely, so GP asserts, breaches by Hideous of its obligations under the Contract in relation to the obtaining of the Planning Permission and in relation to dealing with the Covenant.

- 6.1 GP says that Hideous failed to use reasonable endeavours to obtain the Planning Permission, failed to use best endeavours to deal with the Covenant, and failed to use all reasonable endeavours to ensure that completion of the Contract took place. GP says that if these breaches had not occurred, all of the Conditions would have been satisfied by the Specified Date.

Questions

1. Was Hideous in breach of its obligations under the Contract in relation to the obtaining of the Planning Permission?
2. Was Hideous in breach of its obligations under the Contract in relation to dealing with the Covenant?
3. Was Hideous entitled to terminate the Contract?

Case law

(1) Reasonable, best and other endeavours

Regis Property Co. Ltd v Redman [1956] 2 QB 612

“Finally, it was argued that the form of the covenant as to the supply of constant hot water and central heating was such as to impose no legal obligation on the plaintiffs, inasmuch as they only covenanted to use their best endeavours to maintain the supply of constant hot water and central heating, and were themselves to determine the dates marking the beginning and end of the cold season to which the provision of central heating was to be limited. I do not agree that the covenant imposed no legal obligation. The plaintiffs assumed a legal obligation to do their best.” (Jenkins LJ at 628-629)

Pips (Leisure Productions) Ltd v Walton (1982) 43 P&CR 415

*“I would construe a contract by the parties to “use their best endeavour” to complete a purchase by a given date to mean what it says. “Best endeavours” are something less than efforts which go beyond the bounds of reason, but are considerably more than casual and intermittent activities. There must at least be the doing of all that reasonable persons reasonably could do in the circumstances. I think that this view accords with *Terrell v. Mabie Todd and Co. Ltd.* The question, then, is one of the effect of the words of the contract, thus construed, on time having been made of the essence of the contract by reason of the nature of the subject-matter” (Sir Robert Megarry V-C at 420-421).*

Yewbelle Limited v London Green Developments Limited [2006] EWHC 3166 (Ch)

“It is not suggested in the present case that the obligation to use reasonable endeavours to obtain the section 106 agreement is unenforceable. Mr Bannister submitted that both P & O and Phillips were essentially cases about agreements to agree, and to that extent were unhelpful. I agree that this is a factor that I must bear in mind. However, the essence of the obligation required Yewbelle to use reasonable endeavours to reach an agreement, not with the other party to the contract, but with a third party. To that extent it seems to me that at the very least Phillips is a useful analogy. In using reasonable endeavours towards that end, I do not consider that Yewbelle was required to sacrifice its own commercial interests.”(Lewison J. at paragraph 122).

Yewbelle Limited v London Green Developments Limited [2007] EWCA Civ 475

“The question is whether the position had been reached under which the sellers were entitled to give notice to the buyers to make up their mind. If it had been reached in relation to one factor e.g. the third party land, then the fact that it had not been reached in relation to another factor seems to me irrelevant. The obligation is one composite obligation and if any use of reasonable endeavours is going to fail to produce a compliant agreement then I see no basis on which the sellers would be bound to go on endeavouring to negotiate some other aspect of the agreement.”(Waller LJ at paragraph 126).

Rhodia International Holdings Ltd v. Huntsman International LLC [2007] 1 CLC 59

“I am not convinced that (apart from that decision of Rougier J) any of the judges in the cases upon which Mr Beazley relied were directing their minds specifically to the issue whether “best endeavours” and “reasonable endeavours” mean the same thing. As a matter of language and business common sense, untrammelled by authority, one would surely conclude that they did not. This is because there may be a number of reasonable courses which could be taken in a given situation to achieve a particular aim. An obligation to use reasonable endeavours to achieve the aim probably only requires a party to take one reasonable course, not all of them, whereas an obligation to use best endeavours probably requires a party to take all the reasonable courses he can. In that

context, it may well be that an obligation to use all reasonable endeavours equates with using best endeavours and it seems to me that is essentially what Mustill J is saying in the Overseas Buyers case.”(Flaux J. at paragraph 33).

CPC Group Limited v Qatari Diar Real Estate Investment Company [2010] EWHC 1535 (Ch)

“It seems to me, therefore, that the obligation to use “all reasonable endeavours” does not always require the obligor to sacrifice his commercial interests. In this case, the matter is, however, clearer, because the contract itself, as I have already said, contains other indications that QD was not to be required to sacrifice its commercial interests.

In deed the words of clause 7.1 itself make that clear by using the added words “but commercially prudent” in the phrase “all reasonable but commercially prudent endeavours” (Vos J. at paragraph 252).

Jet2.Com Limited v Blackpool Airport Limited [2012] EWCA Civ 417

“In my view the obligation to use best endeavours to promote Jet2’s business obliged BAL to do all that it reasonably could to enable that business to succeed and grow and I do not think the object of the best endeavours is too uncertain to be capable of giving rise to a legally binding obligation. In my view the promotion of Jet2’s business did extend to keeping the airport open to accommodate flights outside normal hours, subject to any right it might have to protect its own financial interests. Accordingly, I think the judge’s decision on that aspect of the matter was correct. On the other hand, an obligation to use all reasonable endeavours to provide a cost base that will facilitate some essential element of another person’s business seems to me to pose greater problems, because it is much more difficult to identify its content. The words are said to import an obligation to use all reasonable endeavours to enable Jet2 to keep its unit costs (and therefore ticket prices) down by enabling it to use its aircraft in the most efficient manner, but I find them too opaque to enable me to give them that meaning with any confidence. However, it is unnecessary to reach any final decision on that question in the present case” (Moore-Bick LJ at paragraph 31).

(2) Termination of the Contract

Cheall v A.P.E.X. [1983] 2 AC 180

“In the course of the speeches, which are not entirely consistent with one another, [in the New Zealand Shipping case [1919] AC 1] reference was made by all their Lordships

to the well known rule of construction that, except in the unlikely case that the contract contains clear express provisions to the contrary, it is to be presumed that it was not the intention of the parties that either party should be entitled to rely upon his own breaches of his primary obligations as bringing the contract to an end, i.e. as terminating any further primary obligations on his part then remaining unperformed....”(Lord Diplock at page 188).

BDW Trading Limited (T/A Barratt North London) v JM Rowe (Investments) Limited
[2011] EWCA Civ 548

“Although there has been a certain amount of academic discussion as to whether the principle has the status of a rule of law which is imposed upon the parties to a contract almost regardless of what they have agreed, it is now clear as a matter of authority that the application of the principle can be excluded or modified by the terms of the contract and that its scope in any particular case will depend upon the construction of the relevant agreement.” (Patten LJ at paragraph 31).

BDW Trading Limited (T/A Barratt North London) v JM Rowe (Investments) Limited
[2011] EWCA Civ 548

“In the present case the proviso to clause 6.2 which creates the right to rescind is expressly subject to the restriction that notice of rescission may not be served when the party in question is in default of its obligations under clause 6.2. This is the only express limitation on the right to rescind (“save where”) and it raises the issue of whether, as a matter of construction, this operates to exclude any wider disability based on a breach of the Contract which brought about the non-satisfaction of the condition relied upon in the notice to rescind.” (Patten LJ at paragraph 32).

Points to think about

Question 1 - Was Hideous in breach of its obligations under the Contract in relation to the obtaining of the Planning Permission?

1. What was the content of the reasonable endeavours obligation?
2. Was Hideous obliged to pursue the Appeal to a conclusion?
3. Was Hideous obliged to fund a larger Section 106 contribution than originally envisaged?
4. Did the obligation to use all reasonable endeavours to procure completion of the Contract apply? If so, what effect did it have?
5. Does it matter that Hideous had the means to pursue the Appeal to completion?
6. Does it matter that the Appeal had good prospects of success?

Question 2 - Was Hideous in breach of its obligations under the Contract in relation to dealing with the Covenant?

1. What was the content of the best endeavours obligation?
2. Was Hideous obliged to pursue Court and/or Upper Tribunal proceedings to a conclusion?
3. Should Hideous have accepted the offer from the Backward family?
4. Should Hideous have sought to negotiate further with the Backward family, with a view to reducing the price of a release of the Covenant?
5. Does it matter that it was unlikely that Court and/or Upper Tribunal proceedings could have been concluded by the Specified Date?
6. Did the obligation to use all reasonable endeavours to procure completion of the Contract apply? If so, what effect did it have?
7. Does it matter that the Hideous had the means to deal with the Covenant?

Question 3 - Was Hideous entitled to terminate the Contract?

1. Was Hideous in breach of the Contract?
2. If Hideous was in breach of the Contract, what obligation or obligations had been breached?
3. If Hideous was in breach of the Contract, did the New Zealand Shipping principle apply?

4. If Hideous was in breach of the Contract, would completion of the Contract have occurred by the Specified Date, but for such breach of the Contract?

Drafting points for the future

1. There is a difference between (i) reasonable endeavours, and (ii) best endeavours or all reasonable endeavours.
2. The obligation to use endeavours is a last resort, to be used where the achieving of a particular result is not under the control of the parties.
3. Try to avoid open ended obligations to use endeavours. Keep the obligation specific to a particular task or objective.
4. Put as much content as possible into an obligation to use endeavours. If the obligation is intended to include the taking of particular steps or the attempted taking of particular steps, spell this out.
5. When framing an obligation to use endeavours to achieve a particular result separate out those actions which can be made the subject of an absolute obligation, in terms of securing the result, and those actions which cannot be made the subject of an absolute obligation and can thus only be the subject of an obligation to use endeavours.
6. If the obligation to use endeavours includes an obligation to make a financial outlay, spell this out as clearly as possible.
7. When drafting a right to terminate a conditional contract, deal expressly with the application of the New Zealand Shipping principle. Is the principle to apply, or to apply in a qualified form, or not to apply at all? Spell this out.

EDWIN JOHNSON QC

13th March 2014

ANSWER SHEET

1. Was Hideous in breach of its obligations under the Contract in relation to the obtaining of the Planning Permission?

YES:

NO:

2. Was Hideous in breach of its obligations under the Contract in relation to dealing with the Covenant?

YES:

NO:

3. Was Hideous entitled to terminate the Contract?

YES:

NO: