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Commercial Law Update

March 2014

Getting more than you bargained for: Newbury v Sun Microsystems Ltd

Commercial reality tells us that when people are negotiating contracts or concluding deals, their primary focus (indeed, sometimes their only focus) is on winning the "arm-wrestle" on those matters which are of the greatest commercial concern to them at the time of the deal. Although the focus is understandable, case reports appear with alarming frequency which demonstrate that those involved in contractual negotiations ignore the seemingly minor or "ancillary" detail at their peril.

Many people wrongly suppose that they are still in the negotiation phase until they have a neatly bound document sitting in front of their company's managing director for signature. As many people know, often from bitter experience, things are never that simple and anyone involved in sales or negotiations would be better off learning this lesson outside the adversarial setting of a courtroom before a high court judge and with experienced barristers poring over their every misstep or failing.

The case of Newbury v Sun Microsystems [2013] EWHC 2180 is a helpful reminder of the care that needs to be taken when entering into discussions with another party, whether in the context of seeking to resolve or settle disputes or, more generally, in seeking to enter into any contractual arrangement.

Facts

The facts were essentially as follows:

- The claimant made a claim against the defendant for contractual commission ($2m) for year ended 30th June 2009. The defendant subsequently issued a counter-claim for alleged overpayment to the claimant.

- On 3rd June 2013, several days before the trial was due to begin, the solicitors for the defendant wrote to the solicitors for the claimant in the following terms:

    1. The defendant was willing to make an offer to settle the entire proceedings
    2. The defendant would pay to the claimant the sum of £601,464.98 in full and final settlement of the claim and counter-claim plus £180,000 in relation to his legal costs
    3. This would be paid within14 days of this offer being accepted.
    4. Such settlement would be recorded in a "suitably worded agreement".
    5. Subject to acceptance by 5pm that day (although this was subsequently extended to 5.30pm by agreement between the two sets of solicitors)

- The claimant's solicitors contacted the defendant's solicitors at 5.21pm to accept the offer.

- A dispute then arose as to the terms in which the settlement should be recorded. The claimant's solicitors wanted the terms set out in the schedule to the court order to be put before the court whereas the defendant's solicitors did not want the terms attached to a court order as a matter of public record. More pertinently for our purposes, the draft of the agreement produced by the defendant's solicitors included items not included in the letter of 3rd June 2013:

    1. It sought to impose an obligation of confidentiality on the claimant.
    2. It included terms in relation to income tax and national insurance contributions.
    3. It provided for payment within 14 days of the agreement (rather than within 14 days of acceptance of the offer as had previously been stipulated).

- The claimant contended that the defendant's solicitors' "preferred approach" did not record the terms of settlement as stated in the letter of 3rd June 2013. The claimant sought a declaration that a binding settlement agreement had already been reached on the terms set out in the original offer letter.

- The defendant sought to argue that it was not an offer of settlement but an offer to seek to resolve a dispute by indicating the figures they were prepared to agree. A binding agreement would only be reached once the settlement contract document had been finalised.

Judgment

Mr Justice Lewis indicated that the following principles were key to analysing disputes of this nature:

- In order to determine whether a contract has been concluded in the course of correspondence, one must first look to the correspondence as a whole.

- Even if the parties have reached agreement on all the terms of the proposed contract, nevertheless they may intend that the contract shall not become binding until some further condition has been fulfilled. Alternatively, they may intend that the contract shall not become binding until some further term or terms have been agreed.

- Conversely, the parties may intend to be bound forthwith even though there are further terms still to be agreed or some further formality to be fulfilled. If the parties fail to reach agreement on such further terms, the existing contract is not invalidated unless the failure to reach agreement on such further terms renders the contract as a whole unworkable or void for uncertainty.

His decision on the facts was, not surprisingly, that the correspondence of 3rd June 2013 constituted a binding agreement between the parties which settled the claim and counterclaim and set out the terms of the settlement.

- The parties clearly intended to create legal relations and had agreed upon the terms which were essential for the formation of a legally binding agreement.

- The letter from the defendant's solicitors had referred to "such settlement to be recorded in a suitably worded agreement". It did not say "such settlement to be subject to a suitably worded agreement". If it had, this would have been a strong indication that the terms would not be binding until a formal contract was agreed. All that "such settlement to be recorded in a suitably worded agreement" meant was that the objective of the document was for the terms to be "committed to writing as an authentic record" of the agreement already reached.

Lessons

1. **Use of the phrase "subject to contract":** The use of the phrase "subject to contract" in commercial negotiations creates a strong (but not conclusive) presumption that the parties do not yet want to be "in contract". As such, correspondence should in practice always be labelled "subject to contract" until the parties are sure that all terms have been agreed. This is by no means a magic formula and the question of whether or not the expression "subject to contract" is effective to exclude an intention to create legal relations will always be a question of fact.

2. **Choose your words carefully:** As we have seen the defendant thought that indicating that a "formal contract" was "to follow" helped its case when, if anything, the opposite was true. The message is this: the use of "formal" in this context may be taken to indicate that any further document is a mere formality to record the terms of an agreement already reached.

3. **Look before you leap:** It is increasingly the case that negotiations which, in years gone by, would have taken place over the course of several weeks are now concluded over the course of several hours. Often no adverse consequences result from the greatly truncated period for negotiation of settlements but the reality is that it is much harder to pause and consider all of the implications of what is said and written in the course of those negotiations. There is always merit in stopping to think of the wider implications of any particular step or course of action and, in the present context, whether there is merit or value in marking communications as "subject to contract" or a similar form of words.

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