OUTER HOUSE, COURT OF SESSION

[2017] CSOH 112

CA137/14

OPINION OF LORD DOHERTY

In the cause

PROSPECT HEALTHCARE (HAIRMYRES) LIMITED

Pursuer

against

KEIR BUILD LIMITED

Defender

and

CARILLION CONSTRUCTION LIMITED

Third Party

Pursuer: Currie QC, M Hamilton; Harper Macleod LLP
Defender: Lord Davidson of Glen Clova QC, Thomson; Shepherd and Wedderburn LLP
Third Party: Borland QC, MacColl; Brodies LLP

29 August 2017

Introduction

[1] In this commercial action the pursuer sought implement by the defender of a contractual obligation; failing which declarator that it was entitled to be indemnified in terms of the contract between them; failing which payment of damages by the defender for breach of contract. The defender convened the third party and contended that in the event

of the defender being liable to the pursuer, it was entitled to be relieved or indemnified in accordance with the sub-contract between it and the third party. Ultimately the pursuer abandoned the action against the defender in terms of Rule of Court 29.1(2) and duly paid the defender's expenses. The defender did likewise in relation to its claim against the third party. The controversial issue which I had to decide was whether the defender should be relieved by the pursuer in respect of the whole or part of the defender's liability to pay the third party's expenses.

Background

[2] On 27 March 1998 the pursuer entered into a PFI contract with Hairmyres and Stonehouse Hospital NHS Trust ("the Trust"). In terms of that contract the pursuer became obliged to design and construct a new general hospital at Hairmyres and to make the hospital available to the Trust on a continuous basis for a period of approximately thirty years.

[3] On the same date the pursuer entered into a contract (the "Main Contract") with the defender in terms of which the defender undertook to design and construct the hospital. The defender sub-contracted certain elements of the Main Contract works, including hot and cold water piping, to the third party. The piping specified in both the Main Contract and the Sub-Contract was chlorinated polyvinyl chloride ("cpvc") piping.

The Main Contract

[4] In terms of the Main Contract the pursuer was the Employer and the defender was the Contractor. Clause 1.10 of Schedule Part 2 of the Main Contract ("clause 1.10") provided:

> "The Contractor warrants and undertakes that, following the DLP, should the Works be found to suffer from a Structural Defect during the period of 10 years following the DLP, the Contractor shall at its own cost repair, replace or remedy such defects or arrange for such repair, replacement or remedy as quickly as practicable, provided always that the Employer has ensured that such elements have been fully and effectively maintained and cared for by a competent maintenance contractor."

Clause 1.11 of Schedule Part 2 ("clause 1.11") provided that in the event that the Works were found to suffer from a Structural Defect pursuant to the provisions of clause 1.10 the defender should indemnify the pursuer in respect of certain specified consequential deductions made under, or liability actually incurred by the pursuer pursuant to, the provisions of the PFI contract. In terms of clause 1.9.1 of Schedule Part 2 the DLP was defined as 12 months following the issue of the Hospital Commissioning Certificate.

The Sub-Contract

[5] The defender averred that it sub-contracted certain elements of the Works, including the mechanical and electrical installations, to the third party. It averred that clause 3(1) of the Sub-Contract provided that the third party shall be deemed to have full knowledge of the provisions of the Main Contract (other than details of the defender's prices). It further averred that clauses 3(2), 3(3) 3(4) and 13(2) provided:

> "3(2) Save where the provisions of the Sub-Contract otherwise require, the Sub-Contractor shall so carry out, complete and maintain the Sub-Contract Works that no act or omission of his in relation thereto shall constitute, cause or contribute to any breach by the Contractor of any of his obligations under the Main Contract and the sub-Contractor shall, save as aforesaid, assume and perform hereunder all the obligations and liabilities of the Contractor under the Main Contract in relation to the Sub-Contract works.
>
> 3(3) The Sub-Contractor shall indemnify the contractor against every liability which the contractor may incur to any other person whatsoever and against all claims, demands, proceedings, damages, costs and expenses made against or incurred by the Contractor by reason of a breach by the Sub-Contractor of the Sub-Contract.

> 3(4) The Sub-Contractor hereby acknowledges that any breach by him of the Sub-Contract may result in the Contractor's committing breaches of and becoming liable in damages under the Main Contract and other contracts made by him in connection with the Main Works and may occasion further loss or expense to the Contractor in connection with the Main Works and all such loss and expense is hereby agreed to be within the contemplation of the parties as being probable results of any breach by the Sub-Contractor.
> …
> 13(2) After completion of the Main Works or of the section or sections thereof in which the Sub-Contract Works are comprised, as the case may be, the Sub-Contractor shall maintain the Sub-Contract Works and shall make good such defects and imperfections therein as the Contractor is liable to make good under the Main Contract for the like period and otherwise upon the like terms as the Contractor is liable to do under the Main Contract. Provided always that if any defect or imperfection made good by the Sub-Contractor under this sub-clause is caused by the act, neglect or default under the sub-contract of the contractor, his servants or agents, then notwithstanding that the Contractor may have no corresponding right under the Main Contract, the sub-contractor shall be entitled to be paid by the Contractor for his reasonable costs of making good such effect or imperfection."

[6] The third party averred that, in terms of paragraph (B)(a) of the Second Schedule to the Sub-Contract, matters covered by certain design work carried out by Oscar Faber were specifically excluded from the scope of the Sub-Contract Works which the third party was to carry out; and that the third party bore no liability for any defects or imperfections arising from the Oscar Faber design.

The Action

[7] The pursuer averred that the hot water piping was defective and that it required to be replaced, and that as a result a Structural Defect in the Works had become apparent within 10 years of the DLP. It sought decree ordaining the defender to remedy the Structural Defect by replacing the hot water piping system; failing which, declarator that it was entitled to indemnity from the defender in respect of liability incurred by the pursuer to the Trust, and deductions made by the Trust from payments which would otherwise have been due by it to the pursuer but for the Structural Defect; failing which damages of

£11,000,000 in respect of the defender's breach of contract. The action was robustly defended (on the merits, on quantum, and on the ground that the obligations founded on were said to have prescribed). On 18 November 2014 the defender was granted warrant to serve a third party notice on the third party. It duly convened the third party. The defender claimed that in terms of the Sub-Contract it was entitled to relief or indemnity from the third party in the event of the pursuer succeeding against it.

[8] It was common ground that there was evidence of embrittlement of the hot water piping. Up to September 2015 the pursuer's case was that the cause of embrittlement was the migration of phthalate esters from fire collars. It averred that as a result the Works contained a Structural Defect in terms of clause 1.10. On the other hand, the principal position of the defender and the third party was that such embrittlement of the pipework as had occurred was due to natural ageing and that it was not a Structural Defect.

[9] In September 2015 the pursuer produced further reports from its polymer expert, Professor Rimmer, (6/76 of process) and from its engineering expert, Dr Sworder, (6/74 of process). During examination of the cold water piping Professor Rimmer had noted pitting, cracking and cratering. Since there was no possibility of phthalate esters having caused those features Professor Rimmer opined that the upvc piping had been poorly manufactured, and that that was a contributory cause of the embrittlement of the hot water piping. Dr Sworder's further report supported that thesis. Following receipt of the reports the defender and the third party indicated that significant further investigation would be necessary to enable them to respond. On 17 September 2015, on the third party's motion, the October proof diet was discharged. The pursuer was granted leave to lodge a Minute of Amendment. I found the expenses occasioned by the discharge of the proof to be in the cause. I took the view that that was the just course. The situation had arisen because on

examination of the cold water pipework Professor Rimmer had noticed something new which appeared to be significant. I did not consider the pursuer to have been at fault in any respect.

[10] After sundry further procedure, on 16 December 2015 I appointed the proof before answer to take place on 14 June 2016 and the ensuing seven days and on 6 July 2016 and the ensuing six days. Parties had until 27 April 2016 to lodge supplementary expert reports. The supplementary reports prepared by the polymer experts instructed by the defender and the third party put forward a new suggested cause of the embrittlement, namely degradation of a rubber toughening agent and the loss of calcium carbonate. The pursuer sought its experts' views on the new reports. It had difficulty obtaining satisfactory comprehensive responses. Brief written observations were provided by Professor Rimmer and his assistant on 9 and 12 May. The pursuer's experts were then instructed to provide detailed written reports clarifying those parts of their previous reports that they adhered to and those parts of the defender and third party expert reports which they accepted. Unfortunately, Professor Rimmer was not in a position to provide a detailed report as a matter of urgency, but he did provide certain further brief written comments, and he discussed matters orally during the course of a telephone consultation with the pursuer's solicitor and junior counsel. At a consultation with senior counsel on 2 June 2016 it became clear that Professor Rimmer accepted the explanation for embrittlement put forward by the polymer experts for the defender and the third party. He no longer supported the pursuers' case that the causes were the migration of phthalate esters and manufacturing defects. Dr Sworder's views had been predicated to a large extent on Professor Rimmer's reports. Given Professor Rimmer's ultimate view, Dr Sworder was no longer able to support the pursuer's case for the replacement of the hot water piping.

[11] On 8 June 2016 the pursuer intimated that it intended to abandon the action in terms of Rule of Court 29.1(1)(b). An appropriate Minute of Abandonment was lodged the following day. On 13 June 2016, after considering email correspondence from the parties, I discharged the diet of proof.

[12] The pursuer enrolled a motion for its Minute of Abandonment to be received; for the pursuer to be found liable to the defender in the expenses of the action; and for the defender to be appointed to lodge an account of expenses within four months. The third party enrolled a motion for disposal of the third party proceedings on the basis that dismissal be granted provided the defender paid the third party's expenses. The defender enrolled a motion seeking that the pursuer be found liable for the third party's expenses, or that it be found liable to pay the defender a sum equivalent to any part of the third party's expenses for which the defender was found liable. A hearing to dispose of the motions took place on 15 June 2016.

The Hearing on 15 June 2016

[13] At the hearing the pursuer's motion was unopposed. I allowed the pursuer to seek dismissal on condition of paying full judicial expenses to the defender within 28 days of the report of the Auditor on the taxation of the account of expenses of the defender. I found the pursuer liable to the defender in the expenses of process to that date, and I appointed the defender to lodge an account of expenses within four months and ordered it to be remitted when received to the Auditor to tax and report. I certified certain of the defender's witnesses as skilled witnesses.

[14] Senior counsel for the defender moved at the bar to allow it to abandon the claims directed by it against the third party and to seek dismissal of those claims on condition of

paying full judicial expenses to the third party. That motion was unopposed. I allowed the defender to seek dismissal on condition of paying full judicial expenses to the third party within 28 days of the report of the Auditor on the taxation of the account of expenses of the third party. I found the defender liable to the third party in the expenses of process to date as between the defender and third party, and I appointed the third party to lodge an account of expenses within four months and ordered it to be remitted when received to the Auditor to tax and report. I certified certain of the third party's witnesses as skilled witnesses and found the third party's agents entitled to an additional fee. The making of the defender's motion at the bar meant that the third party's motion was no longer necessary (other than in relation to the certification of witnesses and the allowance of an additional fee).

[15] None of those matters was contentious. What was controversial was the defender's motion that the pursuer should bear all, failing which at least part, of the expenses which the defender was found liable to pay to the third party.

[16] Senior counsel for the defender made clear that he accepted that the third party was entitled to recover full expenses against it: that indeed was the defender's motion. However, he submitted that the defender was entitled to be relieved by the pursuer of the whole or at least part of those expenses. It was a fundamental principle that:

> "an award of expenses according to our law is a matter for the exercise in each case of judicial discretion, designed to achieve substantial justice."
>
> (*Howitt* v *W Alexander & Sons Ltd* 1948 SC 154, per Lord President Cooper at p 157).

While an Extra Division of the Inner House in *Albert Bartlett & Sons (Airdrie) Ltd* v *Gilchrist & Lynn & Ors* [2010] CSIH 33 had opined (para 12) that the expenses of third parties are generally only recoverable against the party who has directed a case against them, the court had been careful to stress that that was merely the ordinary rule which might not be

applicable if there had been unreasonable behaviour by a party, or if rights of relief existed. Here, both those exceptions were applicable. First, the pursuer's behaviour had been unreasonable. Its case had been utterly hopeless. The abandonment of the action on the eve of the proof demonstrated that. Second, this was a case where a right of relief ought to exist. Senior counsel was unable to support that proposition by reference to any Scottish authority, but he submitted that in similar circumstances in England and Wales (involving "string" or "chain" contracts) a right of relief was recognised: *LE Cattan Ltd* v *A Michaelides & Co and Ors* [1958] 1 WLR 717, per Diplock J at p 720 and *Friston,* Civil Costs Law and Practice (2nd ed), para 7.47. The defender's action in convening the third party had been reasonable in the circumstances. It had been desirable that the pursuer's claim against the defender and the defender's claim against the third party should be determined at the same time, in the same action, by the same judge. The general rule suggested in *Bartlett* could have the effect of chilling the use of third party procedure. The third party's expenses were very substantial – the estimate at the time of the motion was about £1.6 million. In order for substantial justice to be done here the pursuer ought to be the party who ultimately bore those expenses.

[17] Senior counsel for the pursuer submitted that *Bartlett* was a recent and authoritative exposition by the Inner House of the general rule to be applied when considering the expenses of third parties. Whether or not the law and practice in England and Wales was different, *Bartlett* represented the position in Scotland. The circumstances of the present case did not take it outwith the general rule. The pursuer had not acted unreasonably in pursuing the action, nor had the case been utterly hopeless. Until very shortly before the decision to abandon, the pursuer's position vis-à-vis the defender had been fully supported by its expert witnesses. It was only very shortly before the proof diet that those experts, faced with the supplementary expert reports lodged by the defender and third party,

changed their position. It was not suggested that the defender had any contractual basis for seeking relief from the pursuer in respect of its liability for the third party's expenses, nor was there any other legal basis in Scots law for holding that there was a right of relief in the circumstances. Substantial justice did not demand that relief be granted. The pursuer had not directed the action against the third party. It was not essential that the third party be convened for the defender to defend the action. In fact, the defender had raised separate proceedings against the third party before service of the third party notice. The convening of the third party had increased the number of issues to be determined at the proof and had added substantially to the time and expense involved.

The Decision of 15 June 2016

[18] I refused to grant the relief which the defender sought. I was not persuaded that granting relief was necessary in order to do substantial justice between the pursuer and the defender.

[19] In *Bartlett* the court observed:

> "12. The general rule in relation to expenses is that the cost of litigation falls on the person who has caused it. Thus, in a case such as the present, if the pursuer loses his case, or a material part of it, then he must pay the relative expenses of the other party, since he has caused that other party the expense of vindicating his position. But it follows from the nature of the general rule that the unsuccessful party's liability is limited to paying the expenses of the party against whom he has directed his cause. He cannot be liable, at least in ordinary course and in the absence of some unreasonable behaviour, for the expenses of a party whom he has not introduced into the process and against whom he has directed no case. That is because he has not caused that person to litigate at all. For this reason alone this reclaiming motion must succeed. The expenses of third parties are generally only recoverable against the party who has directed a case against them. There are situations where certain rights of relief exist, but that is not a matter raised in this case."

In my opinion those observations provide recent and authoritative guidance as to the appropriate approach in cases such as the present.

[20] I was not persuaded that there was any good basis for distinguishing *Bartlett* in the circumstances of the present case. I did not accept that there had been unreasonable behaviour on the part of the pursuer. It seemed to me that it had acted properly throughout in accordance with appropriate expert advice.

[21] I was not satisfied that there was any sound basis for holding that the defender ought to be relieved by the pursuer in respect of its liability in expenses to the third party. Senior counsel for the defender acknowledged that there was no Scots authority which supported the existence of a right of relief in the circumstances of the present case. Rather, he urged the court to follow the approach taken by Diplock J in *LE Cattan Ltd* v *A Michaelides & Co and Ors* [1958] 1 WLR 717, at p 720:

> "… I think that I should make these observations about the way in which costs should be dealt with where third, fourth, fifth or sixth parties have been brought in in these string contract cases which are very common. In doing so, however, I want to make it clear that I am not seeking to substitute my discretion for that of the arbitrator, or to suggest that there may not be reasons in some circumstances for making a different order. But, in the ordinary way, where damages are claimed for breach of contract on one contract in a string of contracts, and the seller brings in his immediate seller as a third party, and that party brings in his immediate seller as a fourth party, then, provided that the contracts are the same, or substantially the same, so that the issue as to whether the goods comply with a description is the same, in the normal way the defendant … if successful should recover against the plaintiffs not only his costs but any costs of the third party which he has been ordered to pay; the third party in like manner should recover from the defendant his own costs and any costs of the fourth party which he has been compelled to pay, and so on down the string. That is the normal way in which costs should be dealt with in this kind of action where there is a string of contracts in substantially the same terms. In saying that I am not excluding the possibility that there may be special reasons for departing from that normal practice. Whether it was reasonable for the defendant to bring in a third party at all is always a question to be considered."

Whether or not that is the normal rule in England and Wales, in my opinion *Bartlett*, rather than Diplock J's suggested approach, sets out the principles applicable in Scotland.

[22] I accept that the defender acted reasonably in convening the third party. It was plainly in its interest that its claim against the third party be determined with the pursuer's

claim. However, the pursuer did not introduce the third party into the process, and it did not direct any case against it. It was the defender, not the pursuer, who caused the third party to litigate. In the whole circumstances I was not persuaded that substantial justice required that the pursuer bear all or any part of the defender's liability in expenses to the third party.

[23] While my decision did not turn on the point, I was not convinced that the normal rule in *Bartlett* has a chilling effect on the use of third party procedure. Experience suggests otherwise. On the other hand, a normal rule along the lines described by Diplock J could discourage pursuers from litigating if they ran the risk of incurring liability for the expenses of several third parties further up the contractual chain.

[24] The defender sought leave to reclaim the refusal of its motion that the pursuer be found liable to pay it the expenses which it was liable to pay the third party. I refused leave because (i) the general principles applicable were not in doubt and had been the subject of recent discussion in the Inner House; (ii) the defender would have an opportunity to reclaim when a final interlocutor was pronounced.

Further Procedure and the Reclaiming Motion

[25] The pursuer duly paid the defender's taxed expenses, and the defender duly paid the third party's taxed expenses (which, I was informed on 14 July 2017, were in fact £2.1 million). By interlocutor of 14 July 2017 both the action and the claim set out in the third party notice were dismissed. The defender has marked a reclaiming motion against that interlocutor in order to seek review of the prior interlocutor of 15 June 2016. Those are the circumstances in which this Opinion has been prepared.