



LEGAL BRIEFING

A bit of a misunderstanding

(1) William David Lloyd (2) MGL (Rugby) Ltd v Andrew Michael Sutcliffe (2007)

Court of Appeal, Maurice Kay LJ, Wilson LJ, Sir Peter Gibson [2007] EWHC Civ 153

The Facts

This was an appeal by William David Lloyd (“Lloyd”) and MGL (Rugby) Ltd (“MGL”) against a decision that they were liable to pay Andrew Michael Sutcliffe (“Sutcliffe”) a share of the profit made from a residential building development. Lloyd had, through one of his companies, Nimega Ltd (“Nimega”), obtained two options to purchase the sites of two former petrol stations, and wished to develop those sites. Sutcliffe agreed to carry out the project management, construction and design of the development and make an equal investment into the properties in return for 50 per cent of the share capital and 50 per cent of the profits.

After Sutcliffe commenced work but before a written agreement was made, the parties decided to transfer ownership of Nimega to Lloyd and Sutcliffe equally, with one of the options in respect of one of the sites to be transferred to a new company, MGL, of which Sutcliffe did not have an interest. Lloyd and Sutcliffe entered into a shareholder’s agreement to formalise that arrangement, which included a provision that it reflected the “entire understanding” about “matters dealt with herein”. Significantly, the agreement was silent as to how the profits of the development of the MGL site were to be distributed.

Sutcliffe lent £110,000 to allow the options to be exercised and facilitated the development of the MGL site. However, the relationship between the parties broke down and Lloyd and MGL, relying upon the entire understanding clause, refused to acknowledge that Sutcliffe was entitled to any of the profits from the development of the MGL site. Sutcliffe sued. The trial Judge upheld Sutcliffe’s claim for relief pursuant to the doctrine of proprietary estoppel. Lloyd and MGL appealed.

The Issues

The main issue that arose at trial was whether the “entire understanding” clause in the shareholders’ agreement was triggered such that it dealt with the parties’ arrangements with respect to the MGL site. The second and third grounds of appeal were whether Lloyd and/or MGL could be held liable given that the option was initially in favour of Nimega and property was in fact held by MGL.

The Decision

The appeal was dismissed. In delivering the decision of the court, Lord Justice Wilson held that the entire understanding clause had not been triggered, as it clearly did not dispose of the arrangements between the parties in relation to the MGL site. Indeed, there was only one provision in the shareholders’

agreement that referred to it; namely that the MGL site would no longer be held by Nimega. The arrangements for the development of the MGL site and reference to it were not spelt out. In any event, actions by the parties post-execution of the shareholders' agreement affirmed the earlier profit-share arrangement, and Lloyd and MGL were accordingly estopped from denying the existence of such arrangement.

The second and third grounds of appeal were also dismissed. Prior to the incorporation of MGL, Sutcliffe's understanding as to the profit-share arrangement could only have come from Lloyd personally and there was sufficient evidence that such representations in relation to profit sharing had been made on behalf of, or jointly with, MGL.

Comment

"Entire understanding" clauses (also known as "entire agreement" clauses) are extremely popular in commercial contracts of all types. They are often inserted in an attempt to prevent contracting parties from arguing that pre-contractual representations form part of the contract. This case provides important judicial guidance in relation to the ambit of such clauses; this being an area where such guidance is in short supply.

The decision is perhaps surprising to some, as it shows that the courts will, where appropriate, apply a very strict interpretation of entire understanding clauses and are prepared to look at extraneous evidence (particularly post-execution of agreements containing such clauses) to determine whether they continued to reflect the understanding between the parties up to the date of any dispute.

Parties would be well advised to ensure that important aspects of contractual arrangements are recorded in writing as soon as possible, preferably before getting under way with performance, so as to avoid any later misunderstandings. If contractual arrangements change during performance (as they often do), those changes should be recorded. This case also provides a reminder to those entering into contractual negotiations on behalf of a company yet to be formed that they may be found personally liable for the obligations incurred or representations made on behalf of that company.

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