

Letter of intent

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Charles Blamire-Brown looks at the issues which can surround letters of intent and payment

The contract administrator has issued a letter of intent on behalf of the employer with a limit of ?100,000. The contractor's latest interim application for payment is for ?129,500 + VAT. Is the employer under any obligation to pay more than ?100,000?

Letters of intent can create a veritable minefield of uncertainty. In an ideal world we would all agree contracts up front, setting out the full rights and obligations of the parties without the need for letters of intent. However, this aspiration is not always achievable in practice.

Where a letter of intent is the only viable option, at the very least it should clearly set out the parties' key rights and obligations. One such area is payment, but all too often the issue is insufficiently dealt with. Even with a clearly drafted payment cap, matters on the ground may progress such that additional works are instructed/costs expended, with the result that the originally agreed cap simply does not reflect reality.

Cases

There have been a number of cases where the courts have looked at situations similar to that outlined above. A seminal decision is that in [Mowlem plc v Stena Line Ports Ltd](#) [2004] EWHC 2206 (TCC).

In this case, the contractor's (Mowlem) entitlement to payment for works carried out pursuant to a letter of intent was subject to a cap of ?10m up to 18 July 2003. Additional works were subsequently carried out after this date and Mowlem alleged it had incurred costs over and above the agreed cap. There was a debate on the facts, however, as to whether it could be said these additional works/costs were sanctioned by the employer (Stena).

Mowlem argued it had an entitlement to be paid a reasonable sum for additional works carried out over and above the cap pursuant to an implied term to this effect. Alternatively it argued that:

- it was entitled to a reasonable sum for the works as a quantum meruit
- Stena, by its conduct, had waived its reliance on the cap such that Mowlem would be paid its reasonable costs over and above this cap
- Stena was estopped by convention from relying on the cap and/or denying Mowlem was entitled to a reasonable sum.

The court disagreed, however, and found on the evidence that there was no implied term, nor any estoppel or waiver preventing reliance on the terms of the letter of intent. Mowlem was unable to recover the additional costs it had incurred in spite of Stena's full knowledge that additional works were being carried out over and above the cap.

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The answer to the problem outlined will depend heavily on the facts and the particular drafting of the letter of intent. If the overspend relates to works already within the original scope of works defined in the letter of intent then, absent any agreement from the employer to these increased costs, it is unlikely the contractor will be able to recover them.

However, if the overspend relates to additional works, it will depend in part on the parties' conduct (e.g. in instructing the works). As a general rule, the courts will be reluctant to overturn the commercial bargain of an expressly agreed cap. A contractor is likely to be held to this even if they carry out additional work that gives rise to costs in excess of the cap. It may be possible that the employer's conduct in instructing additional works means that an agreement to go beyond the scope of the cap can be implied and/or the employer is found to have waived their reliance on the cap or is estopped from relying on it.

Best practice

Employers should consider setting a clear financial limit for payment. If they do not wish to be responsible for costs over this limit, they should avoid acting in such a way that it can be inferred they have agreed to costs being incurred over and above the cap. To the extent an employer is aware of additional works being carried out/costs being exceeded over and above the cap, it should make clear in any correspondence that the contractor carries out such works/incurs such costs entirely at its own risk and affirm the existing cap in place.

Contractors should make sure they obtain express instructions and approval from the employer for any additional work and in so doing seek confirmation of its agreement to vary the terms of the letter of intent if they think they will incur extra costs. Further works should not be carried out without such an express agreement in place.

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Further information

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