Inconsistent Contract Terms: Illustrations and Worked Examples

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PRACTICES Energy, Power and Natural Resources, Offshore Oil and Gas, Oil and Gas, International, Shipping

The High Court has recently considered the correct approach to interpreting an "illustration" or "worked example" within a contract when it does not accurately reflect the text it is meant to be illustrating.

In the judgment in *Altera Voyageur Production Limited v Premier Oil E&P UK Ltd* [1], the Commercial Court held that hire due under a charterparty should be assessed in accordance with the worked examples contained in an Appendix, because they provided guidance as to the parties' intention and the contract's true meaning.

The facts were straight-forward. Premier Oil E&P UK Ltd ("Premier"), an oil exploration company, sub-bareboat chartered the FPSO vessel, Voyageur Spirit (the "Vessel"), from Altera Voyageur Production Limited ("Altera"), the operator of the Vessel ("the Charterparty"). There was a dispute in respect of the amount of hire due, caused by an apparent inconsistency of the Charterparty provisions on hire adjustment.

The question before the court was one of construction of the Hire Adjustment Formulae, contained in Section 5 of Appendix M of the Charterparty, which consisted of a narrative and two worked examples. The problem was that both worked examples contained two additional steps which were not expressly set out in the preceding formulae narrative.

Altera claimed that the formulae should be applied precisely in the way set out in the worked examples, resulting in a claim of approximately USD12 million plus interest for unpaid hire. Premier said that Altera's interpretation produced a result which was inconsistent, not only with the preceding narrative, but with the other terms of the Charterparty and commercial commonsense. Premier's reliance on the narrative meant it had a counterclaim for USD3 million for hire it claimed it had overpaid.

It was common ground between the parties that the judgment of Hamblen LJ in *Alexander v West Bromwich Mortgage Co*[2] conveniently summarised the principles which the court should apply in cases where a contract contains an alleged "inconsistency clause", and, the defining features of one: *"to be inconsistent a term must contradict another term or be in conflict with it, such that effect cannot fairly be given to both clauses…inconsistency only arises where the provisions cannot sensibly be read together."*

The only previous judicial discussion on the correct approach of interpreting an illustration which did not fully replicate the preceding text of the contract, was in *Starbev GP Ltd v Interbrew Central European Holdings BV*[3]. In his consideration of the effect of an imprecise illustration in a Sale and Purchase Agreement, Blair J held:

"There is in my view no reason why illustrations or examples should be construed differently than any other contract term in a contract. It could be said in the context of lengthy contracts in financial transactions with much boiler plate that illustrations or examples deserve particular attention as something to which the parties particularly turned their minds."

The inaccurate drafting of the relevant provisions meant that in its attempt to ascertain the objective meaning of the language in which the parties had chosen to express their agreement, the court said it must be wary of focusing too narrowly on the dictionary meaning of individual words and phrases. Instead, the court must look at the terms of any particular provision in its commercial context and against the instrument as a whole.

Even though the court was sympathetic to Premier's submissions and saw that the consequences of its arguments made better commercial sense overall, it could not ignore the agreement that the parties had actually made.

The worked examples were not merely optional extras, but rather, integral parts of the contractual terms which explained how an adjustment was to be calculated, and therefore to disregard them, would be to rewrite the contract that the parties had made.

Further, the court found that in fact, there was no real inconsistency between the worked examples and the narrative. The inclusion of the additional steps in the former, did not mean that they could not be included simply because they were omitted from the narrative. All elements in the hire adjustment mechanism, including the additional steps contained in the worked examples, the court found, were aspects of the way in which the parties had agreed to adjust the hire.

Whilst the Charterparty also included an "inconsistency clause", providing for order of priority in the event of any conflict between provisions, the court held that this was not relevant and had no part to play because there was no real inconsistency.

Moreover, the inclusion of the additional steps in the worked examples, and the apparent commercial illogicality they may cause, was not enough to persuade the court that it was "clear" that something had gone wrong so as to be characterized as "arbitrary and irrational" or as an "obvious nonsense". On the contrary, the court found that it was inherently more probable that the parties' true bargain was to be found in them, as their purpose was to demonstrate with clarity the consequences of the formulae. Applying the principle in *Starbev*, the court found that it is often only when narratives and formulae are worked through that their true effect can properly be seen.

The court relied on the inclusion of the two worked examples as evidence that there was not a mere error and concluded that it was not possible to say that these did not represent what a reasonable person, with all the relevant knowledge, would say that the parties intended should happen.

<u>What can drafters and clients learn from this authority?</u>

The court acknowledged that changes had been made to the Charterparty during drafting, without the consequences always being followed through with rigorous consistency, citing references to non-existent examples and unnecessary repetition in the Appendix. Whilst there is often time pressure during contract negotiations to finalise the deal, care should be taken to ensure that all consequential changes are considered and updated where required. Scrupulous care should be taken to ensure that all provisions, including appendices and worked examples, reflect the parties' agreed intentions.

And what about including worked examples?

Where a contract contains complex formulae, worked examples are undoubtedly useful and can often illustrate far more easily, the practical consequences the parties' intended. But they must be used consistently, taking special care if used with boilerplate clauses, and if they are to be included, consider using more than one to avoid any confusion. However, if the formulae are straight-forward, worked examples may not be required and may even over complicate and confuse matters.

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[1] [2020] EWHC 1891 (Comm)

[2] [2016] EWCA (Civ) 496

[3] [2014] EWHC 1311 (Comm)