[1999–00 Gib LR 329]

CALPE CLEANING SERVICES LIMITED v. ATTORNEY-GENERAL

SUPREME COURT (Pizzarello, A.J.): October 21st, 1999

Documents—interpretation—extrinsic evidence—may examine pre-contractual negotiations to find parties' intentions despite terms excluding extraneous agreement, if necessary to resolve allegation of sham contract—to be construed according to commercial sense, even if parties not previously at arm's length

Contract—repudiation—effect of repudiation—effective when defendant repudiates contract, not when plaintiff accepts breach, though contract continues until acceptance—unilateral declaration of intention to terminate, e.g. press release, is repudiation, and damages payable from that date

Contract—damages—penalty clauses—presumption that agreed sum is pre-estimate of loss if damages difficult to assess precisely—services

contract involving continuing obligation to provide work, including agreement to pay large sum on premature termination, enforceable if no oppression

Contract—illegal contracts—contracts contrary to public policy—private contract unenforceable if fetters Crown's discretionary powers (statutory or prerogative) in future executive action—principle inapplicable to ordinary commercial contracts

The plaintiff brought an action for breach of contract against the Government to recover sums due under a contract for the management and supervision of public works schemes.

The plaintiff was a privately-owned company formed to manage and oversee the performance of public works by workers supplied by the Employment Training Board from among the unemployed. The workers were employed by the plaintiff, and the Government, acting through Government Information Bureau Ltd., paid the plaintiff their wages plus a sum for running costs and profit. *A* and *B*, the plaintiff's company directors, had previously been employed by Government-owned companies performing the same function, and had agreed to run the plaintiff company following negotiations as to their security of tenure and pension rights as employees of the company.

The agreement comprised three contracts: a management service contract for the provision of management and supervision services for the public works schemes by *A* and *B* on behalf of the plaintiff as full-time employees (contract No. 1); a services contract under which the plaintiff would liaise with the E.T.B. to provide for the management and supervisory services and generally to administer the public works schemes (contract No. 2); and a personnel contract providing for the staffing and funding of the schemes (contract No. 3).

Each contract stated that it contained the entire agreement between the parties and superseded any prior agreement. Each provided that in the event of termination "whether by effluxion of time, notice, breach or otherwise" the plaintiff would be entitled to "all arrears of payments due" under the contract "*or* further sums which would but for the determination of [the contract] have fallen due at the end of the term" less a discount for accelerated payment.

Contract No. 1 was stated to be for a term of 10 years, and contracts No. 2 and 3 were for the duration of the public works schemes.

Prior to the signing of the contracts, G.I.B. had made an offer to enter a contract with the company, which *A* and *B* accepted on its behalf, and which obliged the Government to find other services for the company to provide in the event of there being no public works schemes. This provision did not appear in the final contract.

Following a change of Government and a restructuring of G.I.B., the new administration decided that in future public works would once more be undertaken by a Government-owned company, G.P.C. Ltd. The

Government issued a press release stating that it was terminating its contract with the plaintiff on the ground that it could not justify the amount of surplus moneys received by the plaintiff after the workers had been paid. The plaintiff's employees, including *A* and *B*, were, for a limited period, offered the opportunity of employment with G.C.P. Ltd. *A* and *B*, and their spouses (also company directors), had their contracts of employment terminated and registered with the E.T.B. The Government paid one month's salary to the directors and *A* and *B* claimed 13 weeks' unemployment benefit.

The plaintiff formally accepted repudiation of the contract and brought proceedings claiming damages for breach, namely the balance of the payments due under contract No. 1 for the remainder of the 10-year term, as provided for in that contract. No claim was made under contract No. 2 or 3.

It submitted that (a) the defendant's termination of contract No. 1, a fixed term contract, although not a breach of that contract until the plaintiff accepted it, gave rise to the liability claimed; (b) even if contract No. 1 were terminable by notice, the defendant had given the plaintiff no direct notice of termination; (c) contract No. 1 was clearly the main contract, to which the other contracts were ancillary; (d) the fact that *A* and *B*'s spouses were employed as directors to reduce their tax liability did not mean that the entire contractual arrangements between the parties were a sham; (e) the phrase "*or* further sums" (one of several drafting errors by the defendant) had clearly been intended to read "all further sums," and should be so read in order to give the obvious commonsense interpretation to the contracts; (f) alternatively, the *contra proferentem* principle applied in respect of that phrase and it should be construed against the defendant; and (g) the contract fell outside the rule that the Crown could not be fettered by contractual liability in the exercise of its future executive function, as it was a commercial transaction.

The defendant submitted in reply that (a) since remuneration was payable to *A* and *B* only whilst they were full-time employees of the plaintiff and the contracts had terminated only when plaintiff accepted the breach (when they were no longer employed), the plaintiff could recover nothing under contract No. 1; (b) when read together with contracts No. 1 and 2, contract No. 3 (personnel) was clearly the main contract, since contract No. 1 existed only to provide for management and supervision of public works schemes, the other contracts were for the duration of the schemes, and the Government was not obliged to continue them; (c) accordingly, there was an implied term in contract No. 1 that it terminated with contract No. 3; (d) it was clear from *A* and *B*'s employment background and the negotiations leading to the signing of the contracts that the contracts were a sham with the objective of ensuring their continued job security until retirement; (e) furthermore, their duties were personal to them as named employees, the Government funded their salaries as it had previously, their wives were fictitious directors and neither they nor the plaintiff bore any financial risk in the agreement; (f)

the plaintiff's claim was a penalty rather than a genuine pre-estimate of its loss, and *A* and *B* should not be permitted to use the contract with the company (which did not provide for mitigation and which applied whichever party was in breach), to evade their duty to mitigate their loss; (g) the phrase "or further sums" was to be construed as giving an alternative to claiming payment of arrears due under the contract, and not an additional claim; and (h) contract No. 1 was unenforceable on public policy grounds, since it purported to fetter future Governments in the exercise of their executive discretion.

Held, dismissing the plaintiff's claim:

(1) The court was entitled to consider the negotiations leading up to the signing of the contracts as part of the limited factual matrix of the surrounding circumstances known to both parties at the relevant time, which could be taken into account to explain their intentions in entering the agreement. Although at common law, evidence of such negotiations was normally inadmissible in construing an agreement, and the present contracts contained clauses excluding the existence of other terms and superseding previous agreements, there was no other way to resolve the question of whether the agreement was a sham and consequently invalid. The court would aim to construe the agreement in accordance with commercial sense, bearing in mind that the parties had not always operated at arm's length (paras. 40–48).

(2) The relevant background facts included the fact that *A* and *B* wished to protect their job security. The parties had intended that *A* and *B* should not be prejudiced by providing the necessary supervisory services through a private company in the same way as they had in a Government-owned one. Their salaries were therefore protected by a 10-year contract taking them up to retirement age and they incurred no financial risk in the arrangement. The purpose of the contracts had been to enable the Government to deal more advantageously with small public works matters and to attract *A* and *B* to do so by giving them good terms via the company. There was no sham, since the parties had intended the terms of the agreement to have the effect which they appeared to have. There was no ulterior improper purpose. Even if contract No. 3 were regarded as the principal contract (which it was not), the documents were transparent (para. 48; paras. 78–81).

(3) In view of the background to the negotiation of the agreement there was no reason to construe the personnel contract as governing the others or to imply a term that contract No. 1 should lapse if workers were not supplied by the E.T.B. The plaintiff could, *prima facie*, sue under contract No. 1 alone (para. 87).

(4) The proper construction of the three contracts together was hampered by many instances of meaningless or inconsistent phrases

resulting from careless drafting, which the court had to take into account. It would be nonsensical to construe the clause providing for payment of sums which, but for the termination of the contract, would have fallen due under it, as an alternative to recovering arrears of sums already due. The defendant could not elect which to pay (para. 88).

(5) The defendant's press release had plainly been intended to terminate its contract with the company. It had been an anticipatory breach of contract and both parties had acted accordingly. The plaintiff's cause of action for damages arose then, when *A* and *B* had still been employed by the company, and not later when the breach was accepted by the plaintiff. The fact that they continued in employment and were paid afterwards was merely part of the hand-over process and was not to be otherwise interpreted. The measure of damages was the pre-estimate of the loss arising from the premature termination of contract No. 1, prescribed by the contract (paras. 65–67).

(6) Only if contract No. 1 were considered alone could that clause be construed as a penalty, since it included no provision for mitigation of *A* and *B*'s loss through the plaintiff and applied whoever was responsible for the breach of the contract. Furthermore, the fact that *A* would be past retirement age by the expiration of the fixed term and that the contract required them both to be in full-time employment, had not been taken into account (para. 82; para. 84).

(7) However, the defendant had not shown that that clause was a penalty. Reading contract No. 1 together with the others, the parties had knowingly entered an agreement under which large sums would be payable in the event of premature termination. Those sums were not greater than those which ought to have been paid under the agreement. Since the Government's obligation to provide projects for the company was independent of the existence of public works schemes, the intention was that the contract should not necessarily be terminated with the discontinuation of the schemes. In any event, the schemes had continued under the supervision of G.C.P. Ltd. Since damages would be difficult to assess with precision, the sum agreed by the parties was probably an attempt to estimate them. In the absence of oppression, the clause was *prima facie* enforceable (paras. 85–86).

(8) However, the contract—although validly entered into—was unenforceable as a private contract because it purported to fetter the Crown's prerogative powers in the future exercise of executive functions in a matter concerning the welfare of the state (Gibraltar's economic well-being). The Government should not be penalized in contract for its policy decision no longer to engage private companies to oversee public works schemes, since it had to retain its freedom to respond to public need. Although contract No. 1 was not wholly tied to the public works schemes,

the contract could not be honoured without detriment to its policy. The exception in respect of commercial contracts did not apply here, since the contract was a special one executed to give effect to a particular policy of the earlier administration (para. 89; paras. 94–95).

(9) The defendant had, in any event, discharged its burden of showing that the plaintiff had not taken steps to mitigate its loss. Having done so, the burden shifted to *A* and *B*, as the controlling minds behind the company, to show that they had acted reasonably. Despite an offer by the Government of redeployment for all the company's employees, *A* and *B* had shown no real desire to find alternative employment. The court was not convinced of their good faith. The action would be dismissed (para. 104; paras. 109–112).

Cases cited:

(1) *Adams* v. *Cape Indus. PLC*, [1990] Ch. 433; [1991] 1 All E.R. 929.
(2) *Ansett Transp. Indus. (Operations) Pty. Ltd.* v. *Commonwealth* (1977), 17 Aust. L.R. 513.
(3) *Associated Distribs. Ltd*. v. *Hall*, [1938] 2 K.B. 83; [1938] 1 All E.R. 511.
(4) *Bridge* v. *Campbell Discount Co. Ltd*., [1962] A.C. 600; [1962] 1 All E.R. 385, *dicta* of Devlin, L.J. applied.
(5) *Crown Lands Commrs.* v. *Page*, [1960] 2 Q.B. 274; [1960] 2 All E.R. 726, followed.
(6) *Dunlop Pneumatic Tyre Co. Ltd.* v. *New Garage & Motor Co. Ltd.*, [1915] A.C. 79; (1914), 83 L.J.K.B. 1574, applied.
(7) *Elsley* v. *J.G. Collins Ins. Agencies Ltd.*, [1978] 2 S.C.R. 916; (1978), 83 D.L.R. (3d) 1, *dicta* of Dickson, J. applied.
(8) *Gilford Motor Co. Ltd.* v. *Horne*, [1933] Ch. 935; (1933), 102 L.J. Ch. 212.
(9) *Hughes* v. *D.H.S.S.*, [1985] A.C. 776; [1985] I.C.R. 419, followed.
(10) *International Fina Servs. A.G.* v. *Katrina Shipping Ltd. (The "Fina Samco")*, [1995] 2 Lloyd's Rep. 344, *dicta* of Neill, L.J. applied.
(11) *Investors Compensation Scheme Ltd.* v. *West Bromwich Bldg. Socy.*, [1998] 1 W.L.R. 896; [1998] 1 All E.R. 98.
(12) *Kirklees Metrop. Borough Council* v. *Yorkshire Woollen District Transp. Co. Ltd.* (1978), 77 L.G.R. 448.
(13) *Mannai Inv. Co. Ltd.* v. *Eagle Star Life Assur. Co. Ltd*., [1997] A.C. 749; [1997] 3 All E.R. 352, *dicta* of Lord Hoffmann applied.
(14) *Prenn* v. *Simmonds*, [1971] 1 W.L.R. 1381; [1971] 3 All E.R. 237, considered.
(15) *Rederiaktiebolaget Amphitrite* v. *R.*, [1921] 3 K.B. 500; (1921) 8 Lloyd's Rep. 443, applied.
(16) *Roper* v. *Johnson* (1873), L.R. 8 C.P. 167; 42 L.J.C.P. 65.
(17) *Scottish Power PLC* v. *Britoil (Exploration) Ltd.* (1997), 94(47) L.S. Gaz. 30; 141 Sol. Jo. L.B. 246, applied.

(18) *Selvanayagam* v. *University of West Indies*, [1983] 1 W.L.R. 585; [1983] 1 All E.R. 824; (1983), 34 W.I.R. 267, applied.
(19) *Snook* v. *London & West Riding Invs. Ltd.*, [1967] 2 Q.B. 786; [1967] 1 All E.R. 518, *dicta* of Diplock, L.J. applied.
(20) *Staffordshire Area Health Auth.* v. *South Staffs. Waterworks Co.*, [1978] 1 W.L.R. 1387; [1978] 3 All E.R. 769, applied.
(21) *Ward* v. *Newalls Insulation Co. Ltd.*, [1998] 1 W.L.R. 1722; [1998] 2 All E.R. 690.
(22) *Wilson* v. *Wilson* (1854), 5 H.L. Cas. 40; 10 E.R. 811.

H. McGregor, Q.C. and *A. Christodoulides* for the plaintiff;
A.R. Hochhauser, Q.C. and *L.E.C. Baglietto* for the defendant.

1 **PIZZARELLO, A.J.:** The history of this case goes back some years to when the G.S.L.P. Government took over the running of Gibraltar Ship Repair Ltd. ("G.S.L."). Because that company could not be the subject of subsidy from Government, which would run counter to European law, and because it was running at a loss, the Government of the day decided that the core function of G.S.L. would remain with that company and that its ancillary services would be handled by separate satellite companies, each with its own core functions.

2 These companies would be 100% Government-owned and among these was Painting & Cleaning Services Ltd. ("P.C.S.L."), which originated from the paint and cleaning section of G.S.L. It has been referred to as a joint venture company by some of the witnesses but that is a misnomer. Both Mr. da Costa and Mr. Colton were employed by P.C.S.L. at this stage. Mr. da Costa, as manager, received a salary of £22,425 per annum—this was in about 1989—and Mr. Colton's salary was £21,276.

3 It seems that some of these satellite companies worked well but others, amongst which was P.C.S.L., did not and were running at a loss, so gradually P.C.S.L. was run down and lost all its staff, the last employee being Mr. da Costa, who was manager. He found himself involved with Gibraltar Scaffolding Co. ("Scaffolding"), another satellite company which was also not working well. (Mr. da Costa maintained in evidence that he had never been engaged by Scaffolding, but the records show that he was its employee, registered though the Employment and Training Board ("the E.T.B.")). There, Mr. da Costa earned a salary of £16,656.84 as at January 1st, 1993. Mr. Colton had previously moved to Scaffolding in September 1992 as contract manager.

4 In about 1992, the employment situation in Gibraltar was not good and the Government thought up schemes, known as Community Projects Schemes, whereby persons who were unemployed would be employed by a Government-owned company with, as I understand it, three aims: (i) to

provide employment; (ii) to rehabilitate the unemployed; and (iii) so that the working ethos should not be lost.

5 So, P.C.S.L. was brought into play to give a framework to the Community Projects Schemes. Mr. da Costa refers to this as a restructuring of the company. It was not the only company running Community Projects Schemes, but what happened was this. Mr. da Costa was employed as manager, at a salary of £1,719 per month (approximately £20,600 per annum), and his pension rights were protected. This represented, says Mr. da Costa, a drop in salary, but this does not accord with the contract relating to Scaffolding, where his salary is recorded as £16,656.84 per annum.

6 According to Mr. Colton, P.C.S.L. was formed pursuant to this arrangement and he said, as did Mr. da Costa, that it was also permitted to obtain private contract work. I shall refer to this aspect later and it suffices to point out at this stage that Mr. Colton was wrong in his belief that because P.C.S.L. was formed pursuant to the arrangements, P.C.S.L. did not change its character between 1989 and 1995.

7 The workforce for P.C.S.L. was provided by the E.T.B. and so Messrs. da Costa and Colton had little say in the calibre of the workmen employed and could not dismiss any employee. It was therefore difficult for them to control the workers or have them removed. All the expenses were paid by the Government, that is to say, the expenses of administration, *etc*. The E.T.B. is a Government body established under the Gibraltar Development Ordinance 1990.

8 Nevertheless, after a time the experience of the Government was such that it became dissatisfied with this arrangement and consideration was given to a reorganization whereby the work done by P.C.S.L., a Community Projects Schemes matter, would be hived off to a privately-owned company to save the Government expense and time and maximize efficiency. This was some time between late 1994 and early 1995. By this time Mr. Colton was also employed as manager of P.C.S.L. He had been employed to help Mr. da Costa whose workload had increased and he had become ill and unable to cope by himself. Mr. Colton had rejoined P.C.S.L. on November 29th, 1993 and his role was managerial.

9 The Government, for its part, acted through its agent, Gibraltar Information Bureau Ltd. ("G.I.B."). At the material times Mr. Joseph Pilcher, Deputy Chief Minister, was closely involved. He had been tasked by the Government with overseeing the implementation of the Government's ideas. He was not a director of G.I.B. at the outset but his directorship in that company is noted as from April 1st, 1995 and he opened negotiations with the two managers with the intent that a company be formed, 100% privately owned by those two persons who

would carry out the work which Government was doing through P.C.S.L. and which was onerous to it in terms of time and expense.

10 It is right to record that Mr. Pilcher offered Mrs. Beena Purswani (a civil servant attached to P.C.S.L.) the chance to participate in the proposed company but she declined. The new company, it was intended, would be the substitute for P.C.S.L. and would be at arm's length from the Government and in that way the Government would be rid of dealing with the employees directly. Those are the facts as I find them up to this stage.

11 There were, I was told, tough negotiations between Mr. da Costa and Mr. Colton on one side and Mr. Pilcher on the other. Mr. Pilcher, for the Government, wanted to have things done as economically as possible; after all, expense was one of the problems with P.C.S.L. Messrs. da Costa and Colton say they were anxious that they should not lose out on their security of tenure of employment as Government employees or on their pensions. Their security of tenure, whilst not written in stone, was perceived by Mr. da Costa and Mr. Colton to be so, as it was Government policy not to make anyone redundant save on a voluntary basis and, had P.C.S.L. collapsed, they would have been given other employment in another Government-owned company. Their pensions carried from their Government employment through G.S.L. and P.C.S.L. would be frozen, and they would not be entitled to a redundancy payment on termination with P.C.S.L. once they had started with Calpe. They wished to protect for themselves a decent wage and adequate provision for pension, which were two matters Calpe would have to carry.

12 Mr. Pilcher did not put the security of their employment in that way. He said that in fact employees had been treated in that manner by Government but there was no promise of a job. However, he recognized the fears of the two men. In his evidence, Mr. Pilcher explained how he agreed to give the proposed company assets and the use of land, and to arrange with the E.T.B. regarding workers so that the E.T.B. placed employees with Calpe, the Government placed the work, work would be done, G.I.B. would be advised, G.I.B. would pay, G.I.B. was paid by the Government and so G.I.B., a private 100% Government-owned company, would make its profit, as it should as a private concern, and Calpe provided a service the Government wanted. He had not too much recollection about funding and with reference to a cheque for £6,000, he said it was for start-up costs and did not believe it to be a redundancy payment because he could not recollect any redundancy moneys having been paid since some time before Calpe was set up. The contract to cover the salary of both Messrs. da Costa and Colton was for 10 years because, he said, if the Government did not provide Community Projects Schemes they would be left in the lurch, and he obtained the consent of the Council

of Ministers to approve a term of 10 years which would take the two men to retirement age and give them security. If there were no Community Projects Schemes work the Government would provide work for them; meaning, I understood, the two men through the company.

13 Mr. Pilcher's evidence cannot be accepted at face value because in cross-examination he conceded that he could not be precise about the dates and was not to be trusted on details, nor did he explain why if, as P.C.S.L. employees, they were on two weeks' notice they should now have 10 years, other than that it was not intended that the two weeks' notice was to be adhered to in the light of Government's practice with regard to termination of employment. He agreed that the effect was that the Government picked up responsibility and paid through Government funds for salaries and administration costs and the labour through the E.T.B., and that Calpe's role would be essentially to supervise. The directors were to receive pension contributions and overtime. There was no financial risk to Calpe. The practical difference to the Government was that the workers, instead of being employed by a 100% Government-owned company, would now be employed by a privately-owned company and the employees could not run to the Government with any grievance; they would have to sort themselves out with Calpe's directors. He could not recollect what premises were to be used but the Government would not want rent, even though a private company would normally expect to have to pay for premises.

14 The findings of fact I make are these:

(a) Eventually agreement was reached whereby Messrs. Colton and da Costa would form a private company with Mr. da Costa and Mr. Colton as directors, and the company, through them, would handle the work that P.C.S.L. was doing and which would meet the anxieties expressed by Mr. da Costa and Mr. Colton.

(b) A company, Calpe Cleaning Services Ltd. ("Calpe"), was incorporated on February 15th, 1995 and Mr. da Costa and Mr. Colton were appointed directors of Calpe together with their wives. On February 24th, 1995 the Government, acting through its agent, G.I.B., offered to enter into a contract with Calpe, subject to contract, to be drawn up by the Government's solicitors, and on the same day Mr. da Costa and Mr. Colton, as directors of Calpe, accepted on behalf of the company.

(c) Three contracts were drawn up to give effect to the arrangement but neither the directors nor the company sought independent legal advice with regard to the three documents, nor were they advised to, although they were free to do so. They did consult with their lawyers, Messrs. Isola & Isola, peripherally. Messrs. Isola & Isola were also the solicitors for G.I.B. and were the same solicitors who had incorporated Calpe and

helped them in dealings with the E.T.B. The agreements are dated April 5th, 1995 and came into effect on February 27th, 1995.

(d) One contract is the management service contract under which this action is brought. I shall refer to this as contract No. 1. It is for a term of 10 years, terminating on February 27th, 2005. Under it the plaintiff agreed to provide management and supervision services for the Community Projects Schemes, which task was to be carried out by Messrs. da Costa and Colton and they had to be in full-time employment of Calpe. The plaintiff was to be paid £40,235 per annum for its services.

(e) A second contract, to which I shall refer as contract No. 2, is the services contract under which the plaintiff agreed to liaise with the E.T.B. to provide for management and supervisory services for the Community Projects Schemes and generally administer the Community Projects Schemes. The schemes consisted of public works of a cleaning or general labouring nature which were allocated by Government or G.I.B. on an *ad hoc* basis to Calpe. Calpe was issued with these instructions on a daily basis and it would attend to the work that was requested. The plaintiff was to be paid £36,360 per annum, which sum was to be applied to the administration costs, plus the overtime to Messrs. da Costa and Colton, plus the contribution to their pension funds; their directors' basic emolument being covered under the management services contract. This second contract would cover the large expenses the company would have.

(f) A third contract was the personnel contract, to which I shall refer as contract No. 3, which made provision for management and supervision services, the manner in which Calpe would be paid for the employees it supplied for the purpose of carrying out the agreement, and the funding thereby of Calpe in relation to such workers. The defendant was to pay to the plaintiff £93 per week per worker employed. (This was actually settled on a monthly basis). There is nothing in any of the contracts to provide for the further sum of £81 per week per worker which was in fact paid by the E.T.B. to the plaintiff, presumably by arrangement, as explained by Mr. Pilcher.

(g) In respect of each workman there was a contract of engagement entered into between the employee and Calpe and registered with the E.T.B. It is to be noted that both Mr. da Costa and Mr. Colton and their wives entered into such an agreement. Employees covered by the personnel contract were to be paid £128.70 and the difference between £174 (£93 plus £81) was to provide for Calpe's running expenses not covered by the services contract and a margin of profit to Calpe in respect of each worker, so that in very broad terms the more workers it handled the greater was the profit, subject of course, to greater expenditure by Calpe in the provision of more supervisors as the number of workers increased.

(h) The situation while the schemes were run by P.C.S.L. was that the employment of workers was in the hands of the E.T.B. and it controlled the supply of employees. The position *de facto* remained the same with Calpe but is not spelt out in the agreements and the position on the documentation was different because under contract No. 3 it was for Calpe to supply the labourers and at no time was there any documented agreement between Calpe and E.T.B. shown to me or suggested. A further aspect of this arrangement was that Calpe required some capital investment in terms of money, premises, materials and equipment and was given these and a payment of £6,000 each was made to the two directors. The nature of this payment was a matter in issue which I shall deal with later.

15 Calpe started to trade with approximately 30 employees sent by the E.T.B., but by August 1995 there was an increase in the number of persons sent. This was brought to Mr. Pilcher's attention and all went well until May 1996 after the G.S.L.P. Government was replaced by a new administration. Mr. Pilcher wrote to the directors of Calpe on May 24th, 1996. The letter reads:

> "I refer to my meeting with the new shareholders of G.I.B., mainly the Chief Minster, the Hon. P. Caruana, and have been advised that the overall G.I.B. financial structure will be unchanged, although the operational side will change. The different sections within G.I.B. will be reporting to different ministerial structures which, in the case of your section, is outlined below.
>
> Calpe Cleaning Services Ltd. will be under the ministerial portfolio of the Hon. J. Netto and you are therefore to arrange an appointment through his personal assistant, at which stage you should arrange to have Pepe da Costa accompanying you.
>
> The financial structure of G.I.B. will continue in operation and you should therefore report to the Financial Controller, Mrs. Zarb, and liaise with her accordingly.
>
> I would like to take this opportunity to thank you for all the support you have given me and wish you the very best for the future. Could you please pass these sentiments to your staff."

16 As a result, they believed Calpe would be allowed to continue to carry on its business as previously. They had been asked to communicate with the relevant new minister and they say they did and met with him (the Hon. K. Azopardi) in July 1996 when they explained the working of Calpe and some of the problems relating to the employees over the contracts with the E.T.B.

17 I am not persuaded about the accuracy of this, because in his statement Mr. da Costa refers to a July meeting and follows this up by

saying: "We had previously written a letter to him in August advising him that Calpe would continue with the E.T.B. scheme and that we were ready to discuss any new matters with the new Government." Well, one cannot "previously" write in August for a meeting in July, so that throws some doubt on the accuracy of Mr. da Costa's statement, and then there is a letter dated August 30th, 1996 to the Hon. K. Azopardi that makes no mention of a July meeting where one would expect to see it had there been a meeting. Since a meeting with the Chief Minister took place on September 16th, 1996, it does not seem to me that any formal meeting took place with Mr. Azopardi, and I so find. In any case, if there were a meeting it does not seem probable to me that anything seriously affecting either party would have arisen out of such a meeting.

18 However, the new (present) Government, as part of its policy, decided that the public works undertaken by Calpe and S.O.S. 24, another privately-owned company, should either be undertaken by Government-owned companies or the relevant Government Department. To the extent that the Government might still engage private companies to undertake certain public works, such work would be granted pursuant to public tender. So, pursuant to that policy, the Government decided to cease operating the schemes for Calpe and the similar schemes for S.O.S. 24, and to allocate these works to Gibraltar Community Projects Ltd. ("G.C.P."), a wholly-owned Government company.

19 One of the reasons for the policy was that it was considered by the new Government that it would be more economical and less of a burden on the public purse for public works to be undertaken by Government Departments or Government-owned companies or by tender. The Government did not consider that the various amounts paid to Calpe were justifiable or in the public interest. The evidence of Mr. Ernest Montado, the Chief Secretary, further explained the position as perceived by the Government, and I quote from his statement:

> "10. The management services and the services agreements were obviously ancillary to the personnel agreement, since Calpe's obligation was to supervise and manage the personnel engaged in the schemes and provided by Calpe under the personnel agreement. There was, however, no obligation on the Government to organize the schemes for Calpe or similar schemes for S.O.S. 24. Clearly, therefore, the agreements to manage and supervise were only intended to subsist for as long as the Government organized the schemes and/or required Calpe's personnel to undertake them.
>
> . . .
>
> 14. In the case of Calpe, it was felt that there was no justification for Government to remain bound by a 10-year commitment to

engage Calpe to perform management and supervision services, and for the Government to be fettered in its new policy to devolve public works elsewhere. Similar considerations applied as regards the contract with S.O.S. 24."

20 Of course, none of the foregoing was known to the directors of Calpe. Nevertheless, there were discussions between the directors and Government, sparked off by industrial unrest. What had happened was this. S.O.S. 24's workforce was perceived to have been taken over by G.C.P. Ex-S.O.S. 24 workers were on better terms and Calpe's workers were looking for parity with them. When this happened, how it happened and what the position of S.O.S. 24 was with regard to the Government are unclear to me. Mr. Colton says it was on or before August 1996 and Mr. da Costa appears to be of the same recollection but the Branch Officer of the Transport & General Workers' Union on December 4th, 1996 suggests that G.C.P. was not operational until after that date. Nevertheless, the fact is that there were matters causing unrest within the Calpe workforce and Calpe's directors wished to discuss these matters with Government through Mr. Keith Azopardi, the relevant Government Minister. A letter from the Chief Minister to the T.G.W.U., dated September 26th, 1996, confirms that there was unrest and Mr. Colton says they did not meet with Mr. Azopardi at this stage.

21 As I have mentioned, on September 16th, 1996, Mr. Colton attended a meeting on behalf of Calpe, called by the Chief Minister. Mr. da Costa did not attend, as he was on leave. What appears to have been the chief concern at that meeting was a particular problem arising out of the collection of refuse or litter from Irish Town. The Chief Minister thought this was the responsibility of another department or company and he wanted to know why Calpe was doing this—the answer being that under the contract Calpe had been requisitioned to do the job. Mr. Colton went to this meeting with that in mind, but it appears from the documents referred to at the trial that the meeting was not limited to this one topic, for the question of restructuring came up in that meeting, but how substantively I know not. I find as a fact that the question of restructuring came up at that meeting, notwithstanding that Mr. Colton resiled from that admission in the letter when he gave evidence. The letter, he said, was wrong; his statement was correct. I do not accept the accuracy of his evidence on this point. Calpe's own letter to the Chief Minister dated October 1st, 1996 undermines his evidence.

22 After that meeting Calpe continued to function as before and then on October 2nd, 1996 there was another meeting, attended by both Mr. da Costa and Mr. Colton, with the Chief Minister. The purpose seems to have been to discuss how the company functioned and was being run. For their part, the directors were anxious because the workers supplied by the

E.T.B. were no longer covered by their employment contracts, with the attendant problems of income tax and social insurance, and the E.T.B. were not extending contracts in respect of the workers—these contracts being valid for a maximum of 51 weeks' employment—who had been or were being sent to Calpe.

23 The Chief Minister also questioned some work outside the scope of the Community Projects Schemes which Calpe was engaged in, namely, the collection of scrap for which the company was making some £200 per month. I will observe that this is a reference back to P.C.S.L.'s right to obtain private contract work, which advantage Messrs. da Costa and Colton say continued to Calpe's benefit. Mr. Pilcher, in his evidence, said nothing about this. The Chief Minister appears to have told them that he was reviewing the contract but would protect their position with Calpe. According to the directors, the Chief Minister gave no indication of any change in the future and as a gesture of goodwill they agreed to provide him with a copy of the company's accounts.

24 Calpe was then hit by trouble with its workforce. Because S.O.S. 24 had by then been taken over by Gibraltar Community Projects Ltd., the employees of Calpe insisted on parity with the ex-S.O.S. 24 (now G.C.P.) workers having regard to the fact that they had been originally employed on the same sort of terms as themselves. The battle appears to have been between the Government and the employees and in fact there is a letter from the T.G.W.U. dated December 10th, 1996 which reflects this. This had to be so, having regard to the fact that, in essence, Calpe employees were being paid by the Government. Calpe itself could do nothing about the employees' wages.

25 The industrial situation worsened and the workers went on strike. Their pay was increased to £4 per hour as a result of negotiation with the Government to which the directors were not privy (they were told by the union representative in December 1996). On December 20th, 1996 the directors were told by a shop steward that they would be called to attend a meeting with the Chief Minister. The union had a meeting with the Chief Minister on December 20th, 1996 but not with Calpe, whose directors were not called to attend by the Chief Minister. Mr. Pilcher, in evidence, expressed surprise at all this. This problem had never arisen during his term of office and the Government of his day would have refused to entertain any approach by the workers.

26 All this culminated in another meeting with the Chief Minister on January 2nd, 1997, called at short notice on that very day (although the Chief Minister had nominated that date at the meeting of December 20th, 1996, at which Mr. Figueras, the Chief Minister's private secretary at the time, was present and made some notes). Mr. Figueras also took notes of the meeting of January 2nd, 1997. The notes were not official

notes. They were not circulated and were not checked for accuracy with the parties to the meeting. They were exhibited late in the day just before the trial began. Nevertheless, they exist and Mr. Figueras gave evidence to say that the notes were accurate. I shall come to consider the notes later on.

27 On January 7th, 1997 the Government issued a press release which, in my view, terminated its contracts with Calpe, to the consternation of Mr. da Costa and Mr. Colton. This press release reads as follows:

> "The Government is terminating the present arrangements relating to the operation of Calpe Cleaning Services Ltd., a private company owned by its two directors.
>
> The company employs 62 people, who are paid £129 per week. The Government has nevertheless been paying the company £174 per man per week.
>
> The Government is not satisfied that the difference of £45 per man per week, amounting to £145,000 per annum, is justified to meet the other expenses of the Company because—
>
> (a) the Government pays separately and additionally for all materials used by the company; and
>
> (b) apart from the above sums, the Government pays a further £40,235 per annum for the salaries of the directors and £36,396 per annum for other company expenses, including the pension and overtime for the directors.
>
> Accordingly, the company is receiving from public funds a total of £637,000, plus the cost of all materials, per annum, whilst the company's wage bill amounts to only £467,000, plus social insurance, per annum. In the Government's view, these arrangements are not in the public interest.
>
> The Government will therefore discontinue the provision of Community Project Works to the company and will also discontinue the element of wage subsidy provided by the E.T.B. with Government moneys.
>
> The employees of Calpe Cleaning Services Ltd. will be offered employment by Gibraltar Community Projects Ltd. (a Government-owned company) on the same terms as its current employees [the ex-S.O.S. 24 workers].
>
> Employees of Calpe Cleaning Services Ltd. wishing to take up employment with Gibraltar Community Projects Ltd. should collect application forms and draft contracts from Old Sergeants' Mess, 14A Governor's Parade (ground floor) from Wednesday, January

8th, 1997. The offer of employment will remain open for seven days, that is until January 15th, 1997, midday."

28 Matters got considerably worse for the two directors when this press release was followed up by a T.G.W.U. press release dated January 8th, 1997 which suggested that the two directors had short-changed their employees to the tune of £45 per week per person. This was not so and the true position was explained by Government in a later press release dated January 10th, 1997. It seems that the workforce did not pay much heed to the Government's explanation. As a result—and both Mr. da Costa and Mr. Colton say this, and I accept what they say—they came in for a considerable amount of flack, dirty looks, threats, damage to cars, *etc*.

29 In fact, Mr. da Costa and Mr. Colton had acted perfectly properly within the terms of contract No. 3 and Calpe had not short-changed its workers. This is the right moment to mention that Calpe itself issued a press release on January 9th, 1997 (it cannot be January 6th, having regard to its contents) which came under close scrutiny and to which I shall make reference at a later stage.

30 Now, although the Government had terminated the contract of Calpe, nevertheless it arranged for Calpe to pay the workforce until January 17th, 1997 and the offer of employment to the workforce of Calpe was made by Mr. Figueras by a letter to the directors dated January 9th, 1997, pursuant to the terms of the press release of January 7th, 1997. This reads:

"The offer of employment for the employees of your company wishing to take up employment with Gibraltar Community Projects Ltd. ('G.C.P.') is open to them until January 15th, 1997.

The intention is that those persons who do take up the offer will be employed by G.C.P. as from January 20th, 1997. You should continue to pay these employees until G.C.P. takes over."

31 In turn, all Calpe employees had their employment terminated by the company and registered with the E.T.B. with effect from January 17th, 1997 and that included both Mr. Colton and Mr. da Costa ("terminated for remuneration purposes only"). The employment of both their spouses was also terminated and registered with the E.T.B. from January 17th, 1997. Mr. da Costa and Mr. Colton obtained their 13 weeks' unemployment benefit but the two ladies did not, since their employment in the records of the E.T.B. was merely a convenient ploy to lighten the tax liability of Mr. da Costa and Mr. Colton respectively and the ladies were not genuine employees.

32 The amount paid to Calpe in respect of contract No. 1 ("Contract No. 1. One month's contract as agreed for employment with the above

company to Mr. E. Colton and Mr. J. Da Costa"), billed to G.I.B. monthly, was paid to Calpe's account and was then paid out as directors' earnings—£12,231 to Messrs. da Costa and Colton and £8,400 to their wives. As they had not been workers and were therefore not entitled to unemployment benefit, they did not seek to claim this.

33 On January 21st, 1997 Calpe, through its solicitors, gave notice to the Government that it accepted the repudiation of the contract of January 7th, 1997 by the Government and accepted the breach.

34 The plaintiff's claim is for the balance of payments due from the defendant under contract No. 1 for 10 years as at January 7th, 1997, up to and including February 2005, consisting of 98 months at £3,353 per month, making a total of £328,594. Contract No. 1 contains a 5% discount for accelerated payment in the event of termination (cl. 6(a)(ii)), giving a discount of £67,768.47 and so the sum claimed is £260,825.53 plus interest.

35 The plaintiff says that it is entitled to the said payment both because of the defendant's breach, whereupon the balance payable under the fixed 10-year term became payable in full and also because (regardless of the breach) cl. 6 of contract No. 1 expressly provides for such payment. The defendant is clearly in breach, having terminated a fixed-term agreement. Were the court to conclude that contract No. 1 was somehow terminable on notice, such termination, it is submitted, should be on giving reasonable notice and this was not done, the defendant having terminated without notice by way of a public press release. No notice was given directly to the plaintiff.

36 The central matter that I have to consider, having regard to the existence of three separate contracts all drawn up the same day, namely, April 5th, 1995, is which of them is the main contract and if indeed one or other controls the rest. Each contract has two clauses which affect this issue. Both clauses are the same in content in all the agreements. In contract No. 1 the clauses are 8.5 and 8.6 (in contracts No. 2 and 3 the numbering is different) and read as follows:

> "8.5. *Whole Agreement*
>
> Each party acknowledges that this agreement contains the whole agreement between the parties and that it has not relied upon any oral or written representation made to it by the other or its employees or agents.
>
> 8.6. *Supersedes prior Agreement*
>
> This agreement supersedes any prior agreement between the parties whether written or oral and any such prior agreements are

cancelled as at the date on which this agreement shall take place but without prejudice to any rights which have already accrued to either of the parties."

37 Notwithstanding those clauses, the thrust of the plaintiff's case is that contract No. 1 is the principal agreement, while the defendant's case is that put forward by Mr. Montado, namely that contracts No. 1 and 2 are plainly ancillary to the personnel agreement (contract No. 3). It is pleaded that "the management services agreement was ancillary to the personnel agreement and, therefore, entirely dependent on the Government of Gibraltar engaging the plaintiff's personnel in the schemes."

38 One might think that the offer of February 24th, 1995 subject to contract would have placed the contracts in the order of importance as envisaged by the Government; after all it was the Government's offer, through G.I.B. The way the offer is made makes sense with the evidence of Mr. Pilcher, which, in my view, despite some hesitations and corrections, was largely to the effect that there would be work provided for 10 years, more or less until Messrs. da Costa and Colton reached retirement age at 65. That term gave them security and if there was no work the Government would provide some and there should be no financial risk to Calpe.

39 Mr. Pilcher did qualify his evidence by saying that (a) he could not be precise about dates and details and acknowledged that at the time of his negotiations with da Costa and Colton the proper position was that they were subject to two weeks' notice; (b) he was not actually aware of their ages; (c) the employees of P.C.S.L. did not have security of employment; but (d) it was never the intention that the employer's rights in this regard would be exercised.

40 But the matter is not that easy because the existence of the clauses referred to ought to debar my looking at the negotiations leading to those contracts, including the offer of February 24th, 1995, which is clearly marked "subject to contract," and also because, in my view, it is established law that a document has to be construed from within itself as a whole. No notice must be taken of surrounding circumstances save for the facts which are properly admissible as an aid to the construction of the agreement—"the matrix," as defined by Lord Wilberforce in *Prenn* v. *Simmonds* (14) and as referred to in 1978 by Lord Denning, M.R. in *Staffordshire Area Health Auth.* v. *South Staffs. Waterworks Co.* (20) and expounded in *Scottish Power PLC* v. *Britoil (Exploration) Ltd.* (17).

41 Lord Wilberforce said ([1971] 1 W.L.R. at 1385):

"In my opinion, then, evidence of negotiations, or of the parties' intentions . . . ought not to be received, and evidence should be restricted to evidence of the factual background known to the parties

at or before the date of the contract, including evidence of the 'genesis' and objectively the 'aim' of the transaction."

42 Lord Denning, M.R. said ([1978] 1 W.L.R. at 1394–1395):

"Now I quite agree that, if that rule of construction were in force today, Foster J. would be right. There is a great deal to be said for his view that the words 'at all times hereafter' are plain and that they mean 'forever or in perpetuity.' Subtle arguments were adduced before us to limit this meaning. Such as that they meant 'at all times during the day and night,' or 'at all times during the subsistence of the agreement.' But I confess that, as a matter of strict construction, I cannot read any such limitation into the words.

But I think that the rule of strict construction is now quite out of date. It has been supplanted by the rule that written instruments are to be construed in relation to the circumstances as they were known to or contemplated by the parties, and that even the plainest words may fall to be modified if events occur which the parties never had in mind and in which they cannot have intended the agreement to operate.

This modern rule was adumbrated by Cardozo J. in 1918 in the New York Court of Appeals in *Utica City National Bank* v. *Gunn* . . .:

'To take the primary or strict meaning is to make the whole transaction futile. To take the secondary or loose meaning, is to give it efficacy and purpose. In such a situation, the genesis and aim of the transaction may rightly guide our choice.'

The modern rule has recently been expounded with clarity and authority by Lord Wilberforce in the House of Lords in *Reardon Smith Line Ltd.* v. *Yngvar Hansen-Tangen (trading as H. E. Hansen-Tangen)* . . . when he said:

'When one speaks of the intention of the parties to the contract, one is speaking objectively—the parties cannot themselves give direct evidence of what their intention was—and what must be ascertained is what is to be taken as the intention which reasonable people would have had if placed in the situation of the parties. Similarly when one is speaking of aim, or object, or commercial purpose, one is speaking objectively of what reasonable persons would have in mind in the situation of the parties . . . What the court must do must be to place itself in the same factual matrix as that in which the parties were.'

As I understand this modern rule, we are no longer to go by the strict construction of the words as judges did in the 19th century. We

> are to put ourselves in the same situation as the parties were at the time they drew up the instrument—to sit in their chairs with our minds endowed with the same facts as theirs were—and envisage the future with the same degree of foresight as they did. So placed we have to ask ourselves: what were the circumstances in which the contract was made? Does it apply in the least to the new situation which has developed? If events occur for which they have made no provision—and which were outside the realm of their speculations altogether—or of any reasonable persons sitting in their shoes—then the court itself must take a hand and hold that the contract ceases to bind. Such was the rule which I suggested long ago in *British Movietonews Ltd.* v. *London and District Cinemas Ltd.* . . . without success at that time, but which seems to have come into its own now."

43 And in the *Scottish Power* case (17) Staughton, L.J., who delivered the main judgment, with which Otton and Robert Walker, L.JJ. agreed, looked at the structure of the contract, then turned to the background or surrounding circumstances and observed:

> "It has been established law for the greater part of this century that contracts are not construed in a vacuum. The court is entitled to know the surrounding circumstances which prevailed when the contract was made . . .
>
> Equally it is established law first, that subjective evidence of intention by either party is not admissible . . . the court is looking for the *common* intention of the parties . . .
>
> Secondly, evidence of negotiations is not admissible . . .
>
> What then is comprised by the surrounding circumstances, or the factual matrix as the fashionable phrase is today? To my mind it must mean the immediate context of the contract, facts which both parties would have had in mind and known that the other had in mind at the time when the contract was made.
>
> There is little authority on the point . . . In the second appeal I said this:
>
> > 'The boundary of what may be considered surrounding circumstances . . . is unfortunately not easy to draw. All too often a great deal of evidence is produced under that which is of little or no help in interpretation.'"

He finally turned to extraneous facts which were treated as surrounding circumstances.

44 Now, why do I say "*ought to debar* my looking at the negotiations" rather than say "*I shall not* look at the negotiations," which is plainly

what the authorities say? Well, Mr. Hochhauser suggested the following as the proper material background facts:

(a) from November 1993 both men had worked for P.C.S.L.;

(b) P.C.S.L. was Government-owned;

(c) P.C.S.L. had the right to take Government work and outside contracts;

(d) P.C.S.L. was provided by E.T.B. with workmen and paid by Government;

(e) administration expenses were paid or provided by Government;

(f) their functions were to supervise and manage workers on a daily basis;

(g) 10% was paid towards pension by Government;

(h) they were entitled to overtime;

(i) they were earning about £16,600; and

(j) each had a contractual entitlement to receive two weeks' notice of termination.

45 These are certainly background facts, but there are others, in my view, which assume importance and that is because the defendant suggests and pleads that the whole of the transaction is a sham to enable Messrs. da Costa and Colton to draw their wages as previously under P.C.S.L. at no risk to themselves. I think that to determine that question the court will have to look more carefully into the detail of the negotiations which led to the agreements and not restrict itself merely to construing the agreements and that, it seems to me, means looking at the negotiations to consider the reasons why these parties have come together: see *Adams* v. *Cape Indus. PLC* (1) ([1990] Ch. at 538). How else would one be able to conclude the existence of a sham when, on the face of the agreements, there does not appear to be a sham? And should not these facts, thrown up in that investigation, be equally available to the court to help it to construe the contracts? For instance: What regard, if any, has to be paid to the fact that the offer of February 24th, 1995, in respect of contract No. 1, placed an obligation on the Government which does not appear unequivocally in the final agreement as it did in the offer (*i.e.* "in the event of there being no Community Project Scheme requiring the services, the company shall provide such services as the Government of Gibraltar may determine in their absolute discretion")?

46 I should say the following other matters ought to be taken into consideration provided they are determined as facts:

(a) Messrs. da Costa and Colton did not want to prejudice their position in their employment, to the knowledge of the Government;

(b) a 10-year contract would bring them approximately to the usual retiring age of 65;

(c) there was to be no financial risk to the company or the directors; and

(d) the interest of the company was the interest of the directors.

47 I think this approach coincides with the view expressed by Neill, L.J. in *International Fina Servs. A.G.* v. *Katrina Shipping Ltd. (The "Fina Samco")* (10) in quite a different type of case ([1995] 2 Lloyd's Rep. at 350):

> "*The proper approach to the construction of the clause*
>
> It is necessary to remember that this is a commercial document and that one must therefore strive to attribute to it a meaning which accords with business commonsense. Moreover, this approach conforms with the following guidance which can be collected from recent authority:
>
> (1) The fact that a particular construction leads to a very unreasonable result must be a relevant consideration. The more unreasonable the result the more unlikely it is that the parties can have intended it, and if they do intend it the more necessary it is that they shall make their intention abundantly clear [*Wickman Tools v. Schuler A.G.* . . . per Lord Reid].
>
> (2) There must be ascribed to the words a meaning that would make good commercial sense if the [bill of lading] were issued in *any* of these situations, and not some meaning that imposed upon a transferee to whom the bill of lading for goods afloat was negotiated, a financial liability of unknown extent that no businessman in his senses would be willing to incur [*Miramar Maritime Corporation v. Holborn Oil Trading Ltd*. . . . per Lord Diplock].
>
> (3) If detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business commonsense, it must be made to yield to business commonsense [*Antaios Compania Naviera S.A. v. Salen Rederierna A.B.* . . . per Lord Diplock].
>
> (4) Courts will never construe words in a vacuum. To a greater or lesser extent, depending on the subject matter, they will wish to be informed of what may variously be described as the context, the background, the factual matrix or the mischief.

> To seek to construe any instrument in ignorance or disregard of the circumstances which gave rise to it or the situation in which it is expected to take effect is in my view pedantic, sterile and productive of error. But that is not to say that an initial judgment of what an instrument was or should reasonably have been intended to achieve should be permitted to override the clear language of the instrument, since what an author says is usually the surest guide to what he means. To my mind construction is a composite exercise, neither uncompromisingly literal nor unswervingly purposive: the instrument must speak for itself, but it must do so *in situ* and not be transported to the laboratory for microscopic analysis [*Arbuthnott v. Fagan* . . . per Sir Thomas Bingham M.R.].
>
> (5) Dictionaries never solve concrete problems of construction. The meaning of words cannot be ascertained divorced from their context. And part of the contextual scene is the purpose of the provision [*Arbuthnott v Fagan* (supra) per Lord Justice Steyn]."

48 It will be noted that the *Fina Samco* dealt with a commercial document. The instant case is a commercial contract in the sense that it put Calpe at arm's length from Government in their dealings with each other once it was set up, but in so far as that position had been arrived at by a stratagem labelled a "sham" by the defendant, the instant contracts were not the type of commercial document, I venture to suggest, that Neill, L.J. had in mind where the parties had never been anything else than always at arm's length. Nevertheless, I believe the situation in the present case is covered by point (4) in that judgment where the qualification is "depending on the subject-matter." The contracts in the instant case were put forward as a parcel to enable the Government to deal more advantageously with small public works matters, the Community Projects Schemes, and to attract Messrs. da Costa and Colton to do so by giving them good terms via Calpe. That seems to me to be fairly clear and I look behind the corporate veil.

49 Mr. McGregor refers to the three contracts and looking at contract No. 2, he draws attention to the recital which is different to that in contracts No. 1 and 3 and which he submits is palpably wrong. The recital (there is only one recital) in contracts No. 1 and 3 is the same in each and reads:

> "WHEREAS:
> The company is the agent of the Government of Gibraltar and the contractor is a company formed for the purpose of providing management and supervision services . . ."

In contract No. 2 the recital reads:

> "WHEREAS:
> The company appoints the contractor to carry out all such matters as are specified in this contract with effect from February 27th, 1995 until such time as determined in accordance with the terms contained herein . . ."

The proper recital is missing and what purports to be the recital there mimics cl. 1 which is in its right place so that cl. 1 is the same in contracts No. 2 and 3. He suggests the proper recital should be as it is in contracts No. 1 and 3. He also submits there is a senseless expression in cl. 5: "This agreement shall subject to the provisions of cl. 6 below contain a full force and effect until . . ." The words "contain a," he submits, must surely read "continue in" and he offers as an explanation a typist's slip which has gone uncorrected. The reference to cl. 6 in cl. 5, he suggests, should refer to cl. 7. As a result, he submits, there is a strong indication that the contracts were drawn up with a certain lack of care which the court should take into consideration. As to these matters, I unhesitatingly agree with Mr. McGregor.

50 There are other instances of untidiness. In contracts No. 2 and 3 the contract is from February 27th, 1995 "until such time as determined in accordance with the terms contained herein," and yet the termination consequences states: "In the event of the agreement being determined, whether by effluxion of time . . ." a straight copy of contract No. 1, when effluxion of time has no part to play in these contracts. Similarly, in contracts No. 2 and 3, the accelerated payment clause of contract No. 1 finds its way into the termination consequences when it has no place in either contract. In contract No. 3, under "Obligations of contractor," there is a full stop after the word "supply" in cl. 2.1(a) that ought not to be there.

51 Mr. McGregor then turns to a comparison of the three contracts, and notes:

(a) *The different duration terms of the three contracts.* Contract No. 1 reads: "with effect from February 27th, 1995 for a term of 10 years . . ." and "Termination: February 27th, 2005." Contract No. 2 reads: "for the duration of the schemes." Contract No. 3 reads: "for the duration of the schemes," and these periods coincide with the offer. It is self-evident, he submits, that contract No. 1 was a fixed-term contact for 10 years and deliberately so.

(b) *The different termination provisions.* Only contract No. 2 was terminable on notice (cl. 5), namely, three months' notice or one month if there are no Community Projects Schemes. He submits that contract No. 1 is not so terminable.

52 Since it is a fixed-term contract, Mr. McGregor argues that a term as to the termination of the agreement cannot be implied. He refers to Lewison, *The Interpretation of Contracts*, 2nd ed., para. 5.15, at 148 (1997), quoting *Kirklees Metrop. Borough Council* v. *Yorkshire Woollen District Transp. Co. Ltd.* (12):

> "Where the contract is not for an unlimited time, but is for a fixed term, there is likely to be no room for implying further terms as to the termination of the agreement. In *Kirklees Metropolitan Borough Council v. Yorkshire Woollen District Transport Co. Ltd*, an agreement between a company and two local authorities provided that during a period of 99 years neither of the local authorities should operate public transport services. In return the company was to pay the authorities a percentage of its profits. A successor to the company sought to imply a term that the agreement should determine if the company became unable lawfully to operate public transport services. Walton J. held that 'by no stretch of the imagination' could such a term be implied."

53 In so far as the defendant argues that a term ought to be implied into contract No. 1 so that it too, like the two other agreements, was to terminate once the defendant discontinued Community Projects Schemes, that cannot be right, both in terms of the law on implied terms, on the face of the agreements and also in fact, because the evidence is that the defendant has not discontinued the Community Projects Schemes. These are being handled by G.C.P. He refers to 1 *Chitty on Contracts*, 27th ed., para. 13–004, at 620 (1994) as propounding the law correctly:

> "The court will be prepared to imply a term if there arises from the language of the contract itself, and the circumstances under which it is entered into, an inference that the parties must have intended the stipulation in question. An implication of this nature may be made in two situations: first, where it is necessary to give business efficacy to the contract, and, secondly, where the term implied represents the obvious, but unexpressed, intention of the parties."

And in this regard the court should consider that the contracts were drafted by the defendant and, if anything, ought to be construed against it.

54 In applying these principles to the present case, the parties, Mr. McGregor says, were careful to fix the term of contract No. 1 for 10 years. It was specifically for a term of years. The other two are for the duration of Community Projects Schemes. What could have been simpler than to have made the term in the other contracts a term of contract No. 1 if that was what was intended? Furthermore, there is an express termination clause in contract No. 2 (cl. 5(ii) of that contract) and, again,

if the parties had intended this to apply they would have provided for it. There is no room for an implied term. Is it necessary to achieve business efficacy? Consider the purpose of the agreements. What would the officious bystander have said (see *Kirklees* (12))? The fixed term is explicable through and based upon the parties' requirements at the time. Without the guarantee of a 10-year employment the plaintiff's directors would not have been attracted to the defendant's proposals and the 10 years is an express term based on the parties' obvious intentions at the time.

55 Mr. McGregor also turned his attention to the significance of cl. 6(a) of contract No. 1. Contracts No. 2 and 3 have similar provisions in the respective contracts headed: "Termination Consequences." Clause 6, as far as is relevant, reads:

"*Termination Consequences*

In the event of this agreement being determined, whether by effluxion of time, notice, breach or otherwise:

(a) the company shall immediately pay to the contractor:

(i) all arrears of payments due under cl. 3 and any other sums due under the terms of this agreement;

(ii) or further sums which would but for the determination of this agreement have fallen due at the end of the term less discount for any accelerated payment at the rate of five per cent per year . . ."

He argues that the expression "or" occurring after "(ii)" does not detract from the overriding objective that the plaintiff was clearly intended under cl. 6 to be entitled to the balance of the whole sum for 10 years. There would be no point in fixing the contract term at 10 years and providing for a mechanism of accelerated payments in cl. 6 if the defendant's obligations could be simply avoided by an election. What if the contract term expired with large arrears? On the defendant's reasoning, it could elect to pay future sums of which there would be none. That cannot be right, and it renders the meaning of cl. 6 so clear that the plaintiff has no need to fall back on the remedy of rectification. The court has power to correct the obvious: see *Lewison* (*op. cit.*, para. 8.01, at 227).

56 He refers to Lord St. Leonards in *Wilson* v. *Wilson* (22) (5 H.L. Cas. at 66; 10 E.R. at 822):

"Now it is a great mistake if it is supposed that even a Court of Law cannot correct a mistake, or error, on the face of an instrument: there is no magic in words. If you find a clear mistake, and it admits of no

other construction, a Court of Law, as well as a Court of Equity, without impugning any doctrine about correcting those things which can only be shown by parol evidence to be mistakes—without, I say, going into those cases at all, both Courts of Law and of Equity may correct an obvious mistake on the face of an instrument without the slightest difficulty."

57 Also he submitted that the word "or" in cl. 6(a)(ii) could well be a misprint (possibly from dictation) for the word "all" (a misunderstanding which the court appreciates, since I personally misheard "or" and "all" one for the other). The word "all" appears in the same position at cl. 6(a)(i) in contract No. 1, as, indeed, it does in contracts No. 2 and 3. Replacing "all" for "or" in cl. 6(a)(ii) would give the clause the meaning it requires in the context of the agreement and is a common sense interpretation. He refers to Lord Hoffmann in *Investors Compensation Scheme Ltd.* v. *West Bromwich Bldg. Socy.* (11) ([1998] 1 All E.R. at 114–115) and *Mannai Inv. Co. Ltd*. v. *Eagle Star Life Assur. Co. Ltd*. (13), where His Lordship says ([1997] A.C. at 774):

"It is a matter of constant experience that people can convey their meaning unambiguously although they have used the wrong words. We start with an assumption that people will use words and grammar in a conventional way but quite often it becomes obvious that, for one reason or another, they are not doing so and we adjust our interpretation of what they are saying accordingly. We do so in order to make sense of their utterance: so that the different parts of the sentence fit the background of facts which plays an indispensable part in the way we interpret what anyone is saying."

58 Furthermore, he suggests, enlarging on his submission of "all" for "or," that would happily ensure that cl. 6 (a)(i) and (ii) would both start with the same word, and that would make for good drafting because the word "or" to show an alternative would normally come at the end of (i) and not at the beginning of (ii).

59 An alternative argued by Mr. McGregor is that if the court were to find contract No. 1 terminable on notice, such termination would have to be given on reasonable notice. He submits that on the facts of this case the defendant has not given reasonable notice. It terminated the contract by public press release without notice and so is in breach of cl. 8.7. of contract No. 1 in any event. The clause reads:

"*Notices*

Any notice to be served on either of the parties by the other shall be sent by prepaid recorded delivery or registered post or by telefax and shall be deemed to have been received by the addressee within

> 72 hours of posting or 24 hours if sent by telefax to the correct telefax number."

60 Dealing with the alternative, if the court were against him and held that the word "or" implied an alternative, then the right of election, he submits, is the plaintiff's. The clause, on the *contra proferentem* principle, should be construed against the defendant (which is the grantor or proferor, having drafted both the pre-contract letter and the agreements).

61 The first point Mr. Hochhauser makes is based on the pleadings. If he is right that might end the action. The claim, he states, is pleaded in the traditional way, reciting the anticipatory breach of January 7th, 1997 by the issue of the Government press release and the acceptance of that breach on January 21st. The plaintiff's claim is founded on a 10-year contract and if Government prematurely ended contract No. 1 without entitlement that was a breach and that breach was not accepted until January 21st. However, at the end of the trial there was a massive change in the plaintiff's case, and it is now argued that the contract terminated then and there on January 7th and, thus, it was prematurely terminated. That cannot be right, he says, since the unequivocal evidence is the letter of January 21st, 1997, in which the plaintiff accepts the anticipatory breach. It is also contrary to the facts of the case when after January 7th the agreement continued to be performed by both parties when the workers were employed by Calpe until the hand over, employment was terminated on January 17th, 1997 and payments were made to them by Calpe of wages due.

62 The reasons for the change, suggests Mr. Hochhauser, are (a) because as a claim for breach of contract, cl. 6 is not a genuine pre-estimate of loss and (b) the inter-relationship between cl. 2.1(j), cl. 3 and their impact on cl. 6. Clause 2.1(j) reads:

> "(j) ensure that Mr. da Costa and Mr. Colton are in the full-time employ of the contractor. In the event that either or both of them ceases to be in the full-time employ of the contractor for whatever reason the proviso contained in cl. 3 herein shall take effect."

Clause 3 provides for the payment of £40,235 for the services rendered "PROVIDED THAT Mr. da Costa and Mr. Colton are in the full-time employment of [Calpe]" and the impact on cl. 6 is thus that if the acceptance took place on January 21st, then that is when the contract was terminated by breach and at that date Messrs. da Costa and Colton were no longer in the employment of Calpe and so Calpe could recover nothing under the terms of contract No. 1 itself.

63 This, as I understood him, also reflects on the defendant's underlying theme that this was a sham to provide a salary for Messrs. da Costa and

Colton, for an analysis shows that there is no difference in the situation between P.C.S.L. and Calpe, for each operation was free from risk as far as the two men were concerned and each was Government-funded. There is no true realization of private enterprise exposed to the realities of commercial life. It also means, submitted Mr. Hochhauser, that if Calpe is a legal entity, the loss is nil, because the moneys coming into Calpe for the purpose of paying Messrs. da Costa and Colton were not required because after January 17th there was no obligation to pay them. Their employment had been terminated by Calpe.

64 As I understood him in his reply to this, Mr. McGregor agreed with Mr. Hochhauser's analysis that on January 7th there was no breach because one has to wait until it is accepted and then it becomes a breach, *i.e.*, in the instant case, on January 21st, 1997. But his point is that a contract can be terminated without a breach of its terms. He refers to *Associated Distribs. Ltd.* v. *Hill* (3). That, he submits, is what happened here. It is difficult to say there was a breach. There was a termination of the contract without a breach and this gives rise to a liability to pay sums under the contract.

65 It seems to me, on the reading of the Government press release of January 7th, 1997, that the defendant plainly intended not to continue with the contract it had with Calpe. It is not phrased in that way but that is the way I interpret it. I construe that document as an anticipatory breach and both parties have acted on that basis. Until it was accepted, it continued in existence but the cause of action is not the future breach or the acceptance of the anticipatory breach—it is the termination itself, *i.e.* on January 7th, 1997. That is the date one has to look at, and at that date Messrs. da Costa and Colton were in employment, and Calpe is not disentitled to claim on this ground, as was suggested by Mr. Hochhauser.

66 Calpe is, in my view, entitled to damages, which is the normal remedy for the breach of a contract. The measure of that has to be assessed or, as in this case, set out in cl. 6 as a pre-estimate of loss, if, indeed, that is a genuine pre-estimate, which is yet another issue in the instant case which I shall have to consider. I do not believe that Mr. Hochhauser is right to claim in his argument that the proper date is January 21st because that is when the letter accepting the termination was written, or that it is contrary to the facts of the case to accept January 7th as the correct date because the men were employed by Calpe until the hand-over and payments were made in the interim. These are themselves factors which show that Calpe accepted the position created by the termination.

67 It is my view that the obvious intention of Calpe was to smooth the way to a tidy hand-over, and its actions cannot be interpreted, in my view, as anything else. That, I think, is how Mr. Figueras (and presumably the

Chief Minister) saw the matter on January 16th, 1997. If these factors had the effect that Mr. Hochhauser suggests, then the curious situation would arise that the plaintiff could not repudiate on January 21st because it would have accepted the breach and would have had to carry on under the agreement. Otherwise Calpe would be in breach. That cannot be. The conclusion I have arrived at effectively rejects Mr. Hochhauser's submission that Calpe's loss is nil on this ground.

68 Mr. Hochhauser then turned his attention to the three agreements all of which, he submits, should be construed together, and I agree they have to be looked at as a whole. All three are inter-linked and one has to consider the emphasis to be placed on each of them. I have already set out above what Mr. Hochhauser suggests is the matrix on which stand these contracts.

69 Mr. Hochhauser continued that the evidence of Messrs. da Costa and Colton, advanced to flesh out the surrounding circumstances more fully, ought not to be accepted readily because they are not—taking their evidence as a whole—readily believable. One of the matters in their minds was said to be what they had to lose, namely, a guaranteed income. At the time of the Calpe agreement they were earning approximately £16,600, were unlikely to be made redundant and had pensions to which they paid 5% of their salaries and the Government 10%. Both Mr. da Costa and Colton's evidence taken together is that they would not receive redundancy pay on leaving P.C.S.L. to go to Calpe and that their pensions would be frozen. That was false because the evidence is that the pension was not frozen, although they were indeed paying for an annuity while at Calpe for which they were receiving £140 per month under contract No. 2 and they received redundancy payments of £6,000 each from P.C.S.L. and on retirement from P.C.S.L. they received a gratuity of 25% from the Gibraltar Shiprepair Ltd. Provident Fund as leavers. Furthermore, Mr. da Costa was untruthful in his evidence regarding £174 and the 10% of salary paid to him which he said he lost. It turned out that he received £140 towards the pension provided for in contract No. 2, and he deliberately lied despite the clear warning of the judge with respect to the employment of the wives before he finally admitted the truth.

70 Mr. Pilcher's evidence, he argued, also has to be treated with caution, as he was vague about details and admitted that his recollection was that Messrs. da Costa and Colton had received no redundancy, but accepted, when he was shown, that he was wrong and the relevant document was written over his signature. So much of the evidence to support the meaning put forward by the plaintiff must go.

71 Since all three contracts have to be looked at together as a package, Mr. Hochhauser submits that contract No. 1 cannot be looked at in isolation, which is fundamentally what the plaintiff is doing. Thus, what

are the losses which flow from the breach? The defendants say that the assessment at cl. 6 of contract No. 1 is a penalty and not a genuine pre-estimate of loss. In assessing the loss flowing from the breach one has to look at the contracts. There is no claim under contracts No. 2 and 3, yet one must have a look at the benefits available in the contracts. All three of them, and clearly the benefit of contracts No. 2 and 3, are limited to the duration of the schemes, which is precisely what contract No. 1 is all about, notwithstanding that it is a fixed term contract, because the whole point of it is set out in cl. 2.1, especially (a).

"The contractor shall—

(a) provide management and supervision services for the Community Projects Schemes ('the schemes') organized by the Government of Gibraltar ('G.O.G.') in respect of all personnel engaged in the schemes and do so with due care skill and diligence;

(b) not at any time during or after the term divulge or allow to be divulged to any person any confidential information relating to the policies or activities of the company or G.O.G. other than to persons who have signed a secrecy undertaking in a form approved by the company and not permit any person to assist in the provision of the services under this agreement unless such person has signed such an undertaking;

(c) provide such services as the company as the agent of G.O.G. may from time to time reasonably require;

(d) not delegate any duties or obligations arising under this agreement otherwise than may be expressly permitted under its terms;

(e) indemnify and keep indemnified the company from and against any and all loss damage or liability (whether criminal or civil) suffered and legal fees and costs incurred by the company resulting from a breach of this agreement by the contractor including—

(i) any act neglect or default of the contractor's employees or agents,

(ii) breaches in respect of any matter arising from the supply of the services under this agreement resulting in any successful claim by any third party;

(f) maintain at its own cost a comprehensive policy of insurance to cover the liability of the contractor in respect of

any act or default for which it may become liable to indemnify the company under the terms of this agreement;

(g) comply with the terms of any notice specifying a breach of the provisions of this agreement and requiring the breach to be remedied so far as it may be but nothing in this clause is intended to require the company to serve notice of any breach before taking any action in respect of it;

(h) submit audited accounts and such other financial information as may be necessary from time to time to substantiate charges made by the contractor to the company;

(i) immediately upon the termination of this agreement deliver up to the company all correspondence documents specifications papers and property of whatever kind belonging to the company which may be in the possession of the contractor or under the contractor's control;

(j) ensure that Mr. da Costa and Mr. Colton are in the full-time employ of the contractor. In the event that either or both of them ceases to be in the full-time employ of the contractor for whatever reason the proviso contained in cl. 3 herein shall take effect."

And the schemes are set up by the Government with no obligation on the its part to Calpe to keep them going.

72 Thus the composite whole, the framework of the three contracts, does not work unless the Government has schemes and does not pay Calpe except for personnel engaged in the schemes. So it is that looking at the contracts as a whole, the personnel contract (contract No. 3) clearly is for the duration of the schemes and governs the whole edifice and if need be there can and should be an implied term in contract No. 1 to terminate when contract No. 3 terminates "by . . . notice, breach or otherwise." One has also to construe all the issues raised with the overriding premise that there is no financial risk to Calpe, the vehicle used by Messrs. da Costa and Colton for their employment. If one looks at the three agreements it is common ground that there is no minimum obligation on the part of the defendant. It has no obligation to keep up the schemes or devise new ones or to employ any workers. There is not even an obligation on the E.T.B. to supply any labour. That is clear from cl. 3 of contract No. 3. Government could decline any labour it has to certify. The position of Calpe was the same as P.C.S.L., for Messrs. da Costa and Colton were not in a position to determine what their employees' wages would be. "An unusual situation" was how Mr. Pilcher described it and not what was in his mind when Calpe was set up. He wanted to wash his hands of the supervision of the Community Projects Schemes.

73 It is clear, Mr. Hochhauser continued, that contract No. 1 was to provide Messrs. da Costa and Colton with their wages, and the personal element can be seen in contract No. 1, cll. 2.1(j) and 3, pursuant to which da Costa and Colton are to be in the full-time employ of Calpe. In contracts No. 2 and 3, cll. 2.1(k) and 3 are the same. The personal involvement is a theme which runs through all the agreements. Therefore, if, as now, Mr. da Costa is ill and cannot work then that would have a dramatic effect on the contracts and suggests that cl. 6 is not a genuine pre-estimate. When one links these factors up (a) the personal element; (b) Government as the paymaster; and (c) no risk, this is not a genuine privatization but P.C.S.L. under another name.

74 That took Mr. Hochhauser to consider the sham. He submitted that it was a façade, intended to be nothing more than a mechanism for providing a salary for the two men. Hence there is no detail as to how the undefined management services were to be provided and, he submitted, the court should be prepared to break the corporate veil and look behind the façade which concealed the real nature of the relationship between Calpe and Messrs. da Costa and Colton. There is no allegation of fraud or bad faith but, submitted Mr. Hochhauser, there is no need to show that. Contract No. 1 was a glorified employment arrangement between da Costa, Colton and the Government represented by G.I.B. and Pilcher. The evidence is clear from these men. They wished to retain their salary and pension rights, there was no financial investment by the directors in the business, there was no financial risk to them, the Government paid for everything: they were in the same positions as under P.C.S.L.

75 If the contract is held to be a sham then the agreement is unenforceable and the corporate veil should be lifted to prevent Messrs. da Costa and Colton from using the corporate identity of Calpe as a device for evading their legal obligation to mitigate the loss and he refers me to *Gilford Motor Co. Ltd.* v. *Horne* (8) ([1933] Ch. at 961 and 965). Then, in their individual capacity, they would have a duty to mitigate their loss by seeking alternative employment. This they have signally failed to do notwithstanding an offer to them by the Chief Minister at the meeting of January 2nd, 1997 and reiterated in a letter by Mr. Figueras dated January 16th, 1997, which reads:

> "I am writing to ask you to please allow your ex-employees now joining Gibraltar Community Projects Ltd. ('G.C.P.') access to your compound at New Mole Parade so that they can continue with their works after January 20th under the direction of the managers of G.C.P.
>
> In the meantime I wish to give you notice that you are required to vacate the compound within seven days of receipt of this letter. I am asking Mr. Peter Morello of G.C.P. to liaise with you for a smooth transition.

> I would also like to ask you whether you have considered accepting a management post with G.C.P. so that we can discuss terms and conditions if this is of interest to you."

Messrs. da Costa and Colton did not accept the offer, which remains open to this day. They have not taken it up and so by reason of their failure to mitigate they are not entitled to damages.

76 In reply to the allegation of a sham, Mr. McGregor refers me to *Snook* v. *London & West Riding Invs. Ltd.* (19) which considered the meaning of sham in a case where fictitious figures were used: "fictitious figures . . . are badges of sham" said Lord Denning, M.R., and a definition is provided by Diplock, L.J. ([1967] 2 Q.B. at 802):

> "I apprehend that, if it has any meaning in law, it means acts done or documents executed by the parties to the 'sham' which are intended by them to give to third parties or to the court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create. But one thing, I think, is clear in legal principle, morality and the authorities (see *Yorkshire Railway Wagon Co.* v. *Maclure* and *Stoneleigh Finance Ltd.* v. *Phillips*), that for acts or documents to be a 'sham,' with whatever legal consequences follow from this, all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating."

77 The parties intended to enable the plaintiff to administer the Community Projects Schemes with the defendant funding the workers and directors, and removing the administrative burden from the Government, in the way laid down by the agreements. Mr. McGregor observed that in all the cases cited by the defendants there was an advantage the court disapproved of. Devices were used to achieve an improper end, and that is not the case here at all. More importantly, it was open to the Government to act in this way and the company was proposed by the Government. The plaintiffs have disclosed everything and have not hidden behind the corporate veil.

78 I agree with Mr. McGregor. I consider that, notwithstanding an unwillingness on my part to accept the accuracy and truthfulness of the plaintiff's witnesses in everything they say, the essence of the evidence is that the Government and da Costa and Colton entered into this arrangement to provide for the supervision of Community Projects Schemes and their future. It was their common intent that Messrs. da Costa and Colton should not be prejudiced by providing supervisory services via Calpe in the same manner as they had previously with P.C.S.L., that their salary should be protected by a 10-year contract—a

salary which, I should observe, was in excess of the salary which they received at P.C.S.L. (and there was no complaint by Mr. Pilcher that he had been misled about that)—and that there would be no financial risk to Calpe or its directors. All this was known to the parties before the agreements were entered into.

79 There seems to me to be nothing wrong in all that, even though, yes, it means that the operation is free of risk to Messrs. da Costa and Colton; and, yes, there is no material difference in the positions of da Costa and Colton in Calpe from when they were in P.C.S.L.; and, yes, it means that Government provided Messrs. da Costa and Colton with their salary; and, yes, that means that neither Calpe nor its directors are exposed to the realities of commercial life. It is my view that these facts must form part of the background against which the agreements were entered into.

80 In *Bridge* v. *Campbell Discount Co. Ltd*. (4), Lord Devlin said ([1962] A.C. at 634):

> "It is well settled that when a court of law finds that the words which the parties have used in a written agreement are not genuine, and are not designed to express the real nature of the transaction but for some ulterior purpose to disguise it, the court will go behind the sham front and get at the reality."

There is no such ulterior purpose that I can see. The documents are transparent and even if one is to accept the defendant's interpretation that contract No. 3 governs them all (which I do not accept), there is no sham. In that case Lord Devlin made the comment (*ibid*.):

> "That, indeed, is what the court is doing when it declares that what is expressed as an agreement about liquidated damages is not a genuine agreement but cloaks the imposition of a penalty.
>
> . . . I do not see how an agreement can be genuine for one purpose and a sham for another. If it is a sham, it means that it was never made and does not exist; if it does not exist, it must be ignored altogether."

I apprehend this was said in the context of the clause relating to damages itself and does not undermine the whole of an agreement.

81 It seems to me, therefore, that the corporate veil having been parted and the sham of the transaction not having been established, one looks back to the situation of Calpe.

82 Mr. Hochhauser raises this argument. Clause 6 of contract No. 1 is a penalty. It is "extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved and have flowed from the breach": see *Dunlop Pneumatic Tyre Co. Ltd.* v. *New Garage &*

Motor Co. Ltd. (6). It is accepted that whether or not a clause constitutes a penalty must be determined as at the time of the contract. One reason Mr. Hochhauser advances to suggest the clause is a penalty is that the clause has no in-built mitigation in the figures. As I understood him, the claim is made on figures at their highest and the only mitigation is reflected by an accelerated payment of 5%. He suggests that this is the result of pleading the statement of claim on contract No. 1 alone. The clause also appears to entitle Calpe to the sum there referred to even in the event that the agreement were to come to an end by reason of a breach on the part of Calpe.

83 Mr. McGregor, on the other hand, submits that cl. 6 is a genuine pre-estimate of liquidated damages. The point he makes is that contract No. 1 represented only bare salary. The other two contracts provide, in contract No. 2, for pension and overtime and, in contract No. 3, for a modicum of profit, all of which are lost as soon as contracts No. 2 and 3 were terminated. So not only is there a mitigation in respect of the accelerated payments but also if the three contracts are taken together. Mr. McGregor refers me to *Associated Distribs. Ltd.* v. *Hill* (3) and *Bridge* v. *Campbell Discount Co. Ltd.* (4) and *Lewison* (*op. cit.*, para. 15.08, at 433). The sum claimed is not a sum greater than one which ought to have been paid under the contract (one of the criteria set out in the *Dunlop* case).

84 In my view, cl. 6 is not a penalty. If one were to take contract No. 1 alone I think it would inevitably follow that cl. 6 is a penalty, since, apart from the matters mentioned by Mr. Hochhauser, no consideration seems to have been accorded to the fact that Mr. da Costa was 57 at the time the contract was entered into (I should observe that the defendant knew or ought to have known that) and that there was a need for both Messrs. da Costa and Colton to be in full-time employment. Neither would it appear that it takes into account the plaintiff's expected ability to mitigate its loss, the interest of Calpe and its directors being one and the same. The 5% reduction for accelerated payment cannot in my view account for all that.

85 But as I have come to the conclusion below that all three contracts are to be read as a whole, the situation changes. The burden is on the defendant to persuade me that the clause is a penalty clause. Both parties to the contract were aware, on the view I have taken regarding the effect of the termination clause which I set out below, that immediately on the signing of the agreement, reducing as time passed, a large sum could become payable under the terms of cl. 6(a)(ii). It is a contract under seal. It is a contract whereby Calpe undertook under cl. 2.1(c) to provide such services as the company as the agent of the Government of Gibraltar might from time to time reasonably require. This is an independent clause not tied to Community Projects Schemes and I would say that that clause

can also be interpreted as providing for the intention expressed in the pre-contract letter of February 24th, 1995. The discontinuation of Community Projects Schemes for Calpe did not necessarily mean that the contract should be terminated, which termination I have found as a fact happened. And, indeed, the evidence is that the Community Projects Schemes have not ceased: they are being supervised by G.C.P.

86 In the circumstances, I should hazard that damages are difficult to assess with precision, and that strengthens the presumption that a sum agreed between the parties represents an attempt to estimate it, or avoid the expense and difficulty of assessment. I am frankly attracted by the view expressed by Dickson, J. in *Elsley* v. *J.G. Collins Ins. Agencies Ltd.* (7) (83 D.L.R. (3d) at 15) in the Supreme Court of Canada, referred to in 1 *Chitty on Contracts* (*op. cit.*, para. 26–061, at 1252):

> ". . . [T]he power to strike down a penalty clause is a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum. It has no place where there is no oppression."

There is no oppression here on the party having to pay the stipulated amount, namely, the defendant. The stipulation originated from it.

87 Having reached this point, I look back to the central matter that I have to consider. Notwithstanding cll. 8.5 and 8.6 in contract No. 1 and their equivalents in the other two contracts, I shall look at them as one package. I understood both counsel to be agreed on this, and if I am mistaken about that, no matter, because that is my view. I look at the background facts as set out in para. 44 as the material facts. In my view, these are material facts which I can look at, whether or not one looks to piercing the corporate veil. I look at the conclusions I have already arrived at regarding a sham and a penalty. In my view, it is wrong to look at contract No. 3 as governing the situation in the manner advanced by the defendant, and it follows that there is no room to imply a term to the effect that contract No. 1 should lapse if the E.T.B. supplied no workers to Calpe under contract No. 3. The plaintiff is correct in advancing his claim under that agreement. Contract No. 1 can stand apart from the other two. It is also a fixed-term contract which seems to me to give it a slight pre-eminence to the others which are not.

88 I turn to the position under cl. 6. Does "or" mean "all" or does it mean what it says? Both counsel have adverted to the fact that on termination the plaintiff would appear to be entitled to the termination benefits whether or not the contract was broken or terminated by it, even, on the face of it, by the cessation of Messrs. da Costa and Colton's employment in Calpe. Of course, no court would uphold such a claim—

the personal involvement of these two persons is fundamental to each of the agreements. But it means that the court will imply into the agreement something which is not there because it is so obvious. Another instance, if I may say so, of careless drafting. Is it as obvious that "or" means "all"? For the reasons advanced by Mr. McGregor, I have come to the conclusion that he is right and it follows that the arguments placed before me on election fall away.

89 Having come this far, the next question is one that relates to public policy. The defendants argue that contract No. 1 is unenforceable in that it purports to fetter future administrations in the exercise of executive discretion in relation to matters concerning the welfare of the state. The Government, in about December 1996, ceased to organize the schemes and thus ceased to require the plaintiff's personnel to undertake the schemes. This cesser came about as a result of the policy decision of the Government no longer to engage private companies to undertake the works the subject of the schemes, which was part of the wider policy decision of the Government not to engage or fund privately-owned companies to undertake public works or services in cases where the Government did not think it expedient or proper to do so. Accordingly, argues the defendant, when the Government ceased to organize the schemes, as it was entitled to, it incurred no liability under any of the three agreements.

90 Mr. Hochhauser refers to *Rederiaktiebolaget Amphitrite* v. *R.* (15) and also to 1 *Chitty on Contracts* (*op. cit.*, para. 10–007, at 521). In *Chitty* it is stated:

> "**Future executive action.** The power of the Crown (like that of other public authorities) to fetter itself by contract from exercising its discretion is limited, but it is difficult to state the extent and effect of the non-fettering principle with precision. In *The Amphitrite*, Rowlatt J. said that 'it is not competent for the Government to fetter its future executive action which must necessarily be determined by the needs of the community when the question arises. It cannot by contract hamper its freedom of action in matters which concern the welfare of the State.' This statement has been criticised for its width."

91 Mr. Hochhauser also drew attention to *Crown Lands Commrs.* v. *Page* (5) ([1960] 2 Q.B. at 287–289), and I shall quote the relevant parts of Devlin, L.J.'s judgment. He stated (*ibid.*, at 291):

> "When the Crown, or any other person, is entrusted, whether by virtue of the prerogative or by statute, with discretionary powers to be exercised for the public good, it does not, when making a private contract in general terms, undertake (and it may be that it could not

> even with the use of specific language validly undertake) to fetter itself in the use of those powers, and in the exercise of its discretion."

And (*ibid*., at 292) he said:

> "When the Crown, in dealing with one of its subjects, is dealing as if it too were a private person, and is granting leases or buying and selling as ordinary persons do, it is absurd to suppose that it is making any promise about the way in which it will conduct the affairs of the nation. No one can imagine, for example, that when the Crown makes a contract which could not be fulfilled in time of war, it is pledging itself not to declare war for as long as the contract lasts. Even if, therefore, there was an express covenant for quiet enjoyment, or an express promise by the Crown that it would not do any act which might hinder the other party to the contract in the performance of his obligations, the covenant or promise must by necessary implication be read to exclude those measures affecting the nation as a whole which the Crown takes for the public good."

92 The plaintiff's reply is that the doctrine of the *Amphitrite* case does not apply because this court is dealing with a commercial transaction. Mr. McGregor refers me to Lewis, *Judicial Remedies in Public Law*, at 431 (1992). The Crown has an inherent capacity to enter into contracts. The normal rules governing contractual liability apply to the Crown but there are special areas here. Special principles apply to Crown contracts one of which is governed by the principle of the *Amphitrite* case (15), namely, where it is necessary for the Government to retain its freedom of manoeuvre but "ordinary commercial contracts were said to be unaffected by this rule. The exact scope of the principle remains uncertain." In the *Amphitrite* case, Rowlatt, J. said ([1921] 3 K.B. at 503):

> "All I have got to say is whether there was an enforceable contract, and I am of opinion that there was not. No doubt the Government can bind itself through its officers by a commercial contract, and if it does so it must perform it like anyone else or pay damages for the breach. But this was not a commercial contract . . ."

93 As for *Crown Lands Commrs.* v. *Page* (5), that is distinguishable, he says, because this contract was not entered into pursuant to powers under statute. The same point was made by Mason, J. in *Ansett Transp. Indus. (Operations) Pty. Ltd.* v. *Commonwealth of Australia* (2) (17 Aust. L.R. at 530). What was done was indeed an integral part of Government policy but there was no statutory duty to do so. So the instant case is not the type of case envisaged by *Page*.

94 I have come to the conclusion that the agreements were validly entered into, but on this point of fetter, the contract is unenforceable

under the doctrine of the *Amphitrite* case. In my view, although the contract is not wholly tied to the Community Project Schemes the Government could not honour its agreement with Calpe in contract No. 1 with no detriment to its policy—this applies to and affects cl. 2.1(c). The fact that the Community Project Schemes still exist does not seem to me to be relevant to this aspect of the case, for the schemes are now carried out by a company organized within the parameters of Government's policy. That policy is a policy which deals with the economic well-being of Gibraltar and the policy change is in the public interest and hence the welfare of the State.

95 Furthermore, although this is a commercial contract, I have already indicated above that this was a special contract conceived and executed for a particular purpose to give effect to a particular policy of an administration which policy has been changed by a different administration. *Page* (5), as Mr. McGregor submitted, is not wholly on point, as that case dealt with powers exercised under a statutory provision. Nor is *Hughes* v. *D.H.S.S.* (9), which was not referred to directly by counsel but which is referred to in 1 *Chitty on Contracts* (*op. cit*., para. 10–008, at 522–523). In my view, both these cases nevertheless provide comfort for my conclusion, although they deal, as did *Ansett*, with statutory powers and here I am dealing with prerogative powers exercised by the Government on behalf of the Crown.

96 That really should dispose of the case. Nevertheless, for the sake of completeness, I shall refer to mitigation of damages. The burden is on the defendant to show that the plaintiff has failed to take steps to mitigate his damage: see *Chitty on Contracts*, (*op. cit.*, para. 26–051, at 1242–1243), referring to *Roper* v. *Johnson* (16). Once the defendant has discharged this onus (which is a matter of fact) then *Selvanayagam* v. *University of West Indies* (18) shows that the plaintiff is obliged to behave in a reasonable manner and in the instant case the duty of the company so to do falls on the directors. The evidential burden shifts. I have looked behind the corporate veil and the one is the same as the other. The duty to mitigate by Calpe is the duty of the directors who manage the company and who are responsible for carrying the works for which the company is employed under the agreements with G.I.B.

97 The defendant says three things in mitigation. The first is that the onus is on the plaintiff. I disagree, as stated above. The second is that if Calpe is the true contracting party and if the corporate veil is sustained, then there is no loss, because Calpe "for remuneration purposes only" has terminated the employment with it of Messrs. da Costa and Colton, and so it has mitigated its loss to nil. The third is that if the corporate veil is lifted, then (i) at all material times there was alternative work at G.C.P.; (ii) they should have taken it and their refusal entitled them to nothing;

(iii) they cannot hide behind the corporate veil and Calpe did mitigate; and (iv) the account of the steps they have taken to mitigate is untrue and not to be accepted.

98 Note, says Mr. Hochhauser, their actions throughout all the stages of this saga:

1. The whole of their wives' employment was a sham within the enterprise itself. It was fictitious. It bears the mark of dishonesty. They were not employees in real terms, but merely for tax benefit and to pull the wool over the eyes of the E.T.B., and da Costa lied on oath on this aspect.

2. Da Costa's pension hardship argument which is not borne out by the pay-slip of May 31st, 1993.

3. The claim that they were receiving a salary of about £20,000 with P.C.S.L., when in fact they were getting approximately £16,600 in 1995, as evidenced by the pay-slip for April 30th, 1995.

4. The claim that they had received no redundancy payment when they left P.C.S.L., which was false.

5. The claim that their pension was frozen, which was false.

6. Their statements that they were continually pressing for a meeting with the Chief Minister.

99 Ignore, he says: (a) the meeting of September 16th; (b) their letter of October 1st, which refers to their knowledge of restructure plans which Colton was unable to explain away in evidence and that at the meeting of October 22nd, Mr. da Costa records that meeting was "a friendly meeting" and Mr. Colton "no bitterness," but in evidence they stated that the Chief Minister said if they were going to be political he would sack them all; (c) their protestation that they had no clue of what was going to happen, which is at odds with their press release issued a week later on January 9th, 1997. It is interesting, Mr. Hochhauser says, that after the meeting of January 2nd there is an absence of any letter complaining of arrears or seeking clarification of Mr. Figueras's letter of the 16th, in view of the contents of that press release, which stated:

> "In their last meeting Mr. Caruana informed them that it was his intention to transfer the employees and the operation to a Government Company and employ the two directors in the new operation with the same terms and conditions as those of their contract."

When Mr. Figueras wrote on January 16th it was in the context of the Chief Minister's intention, communicated and known to the directors, as admitted in their press release. That was an offer. It was a sincere

proposal and it was rejected. Their reply was by letter dated January 21st, 1997: "The company will consider all proposals in mitigation of its claim for damages which the Government may care to put forward including any offers relating to the provision of services by the directors."

100 Note further, says Mr. Hochhauser:

7. Up to mid-February they say they were willing to take up employment, but they had made no effort to contact Mr. Figueras, if Mr. Figueras is to be believed. Nor had they made contact with Mr. Morello. And why? Because they believed they were on a winner under cl. 6, as they had indicated at the meeting and identified in Figueras's notes.

8. They were making things up as they went along and the documents showed them up.

9. They made no attempt to mitigate. Mr. da Costa is not interested in work. His evidence about his heart attack lacked certainty and detail, and Mr. Colton has ceased to look for work. On January 21st, 1997 they wrote to offer their services and yet they said in evidence that they could not accept because of all the hassle they received at the time. Well, their contact with the workers had ceased on January 17th, and the situation on the 21st was the same as it is now. What credibility is there in what they say?

101 On the other side of the coin, the plaintiff says that there was no offer to integrate the directors of Calpe into a new job. The letter of January 16th, 1997 cannot be regarded as an offer (possibly as an invitation to treat, but nothing more), and the directors did try pursue the matter but came to a dead end when the attempts to get in touch with Government officials on the telephone were not acknowledged at the time. Mr. Morello, who was being approached by them as a conduit to Government on a daily basis, since Morello was using their site and materials, did not help in any way. The situation is that the defendant did not pursue the matter and the onus is on it. What evidence is accepted as credible depends on the view the court takes of the witnesses.

102 Mr. McGregor submits that the only issue that can properly be taken against Mr. da Costa and Mr. Colton is the false evidence they supplied in respect of the employment of their wives. Other than that they are honest men. Their attempt to ameliorate their tax position is comprehensible and may not be wrong: see *Ward* v. *Newalls Insulation Co. Ltd.* (21). In respect of the redundancy payment, that should not be held against them as a falsehood. Mr. Pilcher himself thought that payment was made not for redundancy but as a start up, which is what the money was used for. In respect of the employment at Scaffolding, it is clear that those companies were in a state of flux and Mr. da Costa's employment there could not have been for long. The E.T.B. form shows his engagement on January 1st, 1993 and he was receiving salary from

P.C.S.L. from April 1993 onwards, as shown from the pay-slips. Furthermore, they did try find work with the E.T.B. after the 13-week unemployment period. Now there is an offer, but they do not want to take it and that is reasonable in the circumstances, in view of the harassment they have received from workers whom they would now have to supervise if they accepted the offer—workers who will have lost respect for them—and then they would have to work with and probably under Mr. Morello, the same person who has behaved badly towards them.

103 Turning to the defendant's points, I think Mr. Hochhauser is right that if one does not break the corporate veil then there is no loss to Calpe. But I have pierced the corporate veil and the first point to consider is whether the defendant has discharged its onus to show that the directors have failed to mitigate. If one looks at the letter of January 16th, 1997 in isolation then I would agree with Mr. McGregor that the letter does not amount to an offer, but it is a letter which follows a certain amount of discussion with the Chief Minister, scattered over a period of months—from September 16th, 1996, to be precise, when the matter of restructuring had, in my view, been advanced by the Chief Minister. This was followed by the meeting in October and the developments regarding the workers' pay and conditions in conjunction with the S.O.S. 24 situation, in respect of which Messrs. da Costa and Colton seem to have been singularly omitted but which matters, however, can scarcely have gone unperceived by them. The meeting of January 2nd, 1997 gave the clearest indication (accepted by them in their press release) that there was going to be change and that they were to be offered comparable posts at comparable rates.

104 A point I would make is that the notes of Mr. Figueras, in my view, indicate that on January 2nd the Chief Minister had yet to decide on what is now stated to have then been Government policy. At the very least, the Chief Minister seems to have beaten about the bush rather than told them outright. For instance, he indicated that he wanted a week to look at the contracts, if Mr. Figueras's notes are accurate. The important point, though, is that, at any rate, it was clear to da Costa and Colton that—to quote again the words of their own circular written at a time when there was no reason not to be accurate—

> "in their last meeting Mr. Caruana informed them that it was his intention to transfer the employees and the operation to a Government company and employ the two directors in the new operation with the same terms and conditions as those of their contract."

Despite the fact that the Chief Minister had suggested waiting a week, and while it is obvious he did not (the press release was issued five days later), it seems to me that the defendant had done as much as was in its

power to ensure that the directors did have an opportunity to take up the Chief Minister's stated intention, and the letter does amount to an offer.

105 The offer was not accepted because, by a letter dated January 21st, Messrs. da Costa and Colton issued their own invitation to treat, thereby showing an intent on their part to mitigate damages. Further, on January 23rd, 1997 they asked the Administrative Secretary whether the Government was prepared "to enter into discussion with a view to an amicable settlement," and so it is correct to say that the defendant did not reply and made no formal invitation until recently.

106 One thing that bothers me is that Messrs. da Costa and Colton say they went to the E.T.B. for work and nothing was available for them. That evidence was basically unchallenged and it strikes me that if the Government did have this offer open, why was the E.T.B. unaware of it? There is no evidence that the E.T.B. steered the two men in that direction and of course the E.T.B. would not have known unless told by some Government official that this employment was available for both men. I draw an inference against the defendant that it was not particularly bothered to have these two men re-employed by it or any company controlled by it.

107 Where does this leave the onus? Has the defendant discharged its onus sufficiently to exonerate it from doing anything more? Well, we have it from Messrs. da Costa and Colton that they tried to get in touch with Mr. Figueras, and Colton says that on one occasion he did speak to Mr. Figueras and that that gentleman lied when he denied the conversation in which, Colton said, Figueras refused to set up a meeting with the Chief Minister. If true, that would be evidence that the defendant had not discharged its onus, but if that had happened, would they not have raised it in their letter to the Chief Minister of January 14th? They also say that they spoke to Mr. Morello daily and that Morello has not been truthful when he states that he never saw the directors after January 16th. There is only a letter from Mr. Morello on this, dated February 4th, 1997, exhibited by Mr. Figueras, so I do not have the benefit of Mr. Morello's evidence and so I put it to one side.

108 There is also the evidence of Mr. Figueras in relation to his notes, where he records da Costa as suggesting "if integration, not interested." One of the two says of that record that it is not true and the other says that Mr. Figueras made it up. And that went for some other parts of Mr. Figueras's record. In general terms, both da Costa and Colton said parts were inaccurate—Mr. Colton is hardly recorded as speaking, whereas they say he had his say but they spoke in Spanish, which is not recorded—parts are untrue, and they accept certain parts as correct.

109 When tested in cross-examination, their points of difference with the record did not always coincide, and I did not take that as a sign of genuine misunderstanding. The view I have formed, having heard them in the

witness-box, is that I should place no confidence in their evidence. Where their evidence conflicts with that of Mr. Figueras, I accept Mr. Figueras's. Mr. Hochhauser drew a lot of strands together which I have recorded above, and while I do not accept them all, I do accept the majority, and they are more than enough to cause me to doubt their good faith.

110 There are other instances:

(a) The evidence that they were paid their salary at Calpe three months in advance in a lump sum, which commenced on February 27th, 1995, yet they were paid also by P.C.S.L. at end of April 1995.

(b) They claimed for the stock in trade of Calpe to the tune of £31,428,50. Where did this come from? Mr. Pilcher's evidence was that the Government would provide Calpe with stock and materials, and even if bought from the profits of the company all that would have come from moneys actually received from Government. They appear to me, basically, to be claiming from Government that which came from Government in the first place. Accepted, it was their company and they could do what they liked, in the same way as they appointed directors and distributed the moneys received from G.I.B. for their directors' fees among themselves and their wives. These matters do not add up to acting in good faith. True, they say that they ploughed in £12,000 as start-up funds and they would have been entitled to reimburse themselves, and they had that scrap-metal sideline which was worth £200 per month, but where were the company accounts to justify this?

(c) Their notice of termination to the E.T.B. and the explanation that that had to be done to get unemployment benefit are shades of another sham. I am sceptical of their intent and, on the whole, considering all these matters together, I have come to the conclusion that neither Mr. da Costa nor Mr. Colton has any genuine desire to mitigate his damage. They are looking to get as much as possible out of their agreements. The long and short of it is that I am persuaded that the defendant has in fact discharged its burden of proof.

111 Is it reasonable for the directors to refuse to take up the employment on offer? In my view, no, if they were willing in January 1997 and the situation now is no different to what it was then. I heard their accounts of bad times. I am prepared to accept that this happened, but it will have blown over. Besides, the evidence was that Calpe's workforce was comparatively small compared to that of S.O.S. 24, so that G.C.P.'s workforce that took over S.O.S. 24 will have had, in January 1997, and now has, a large number of workers with whom Messrs. da Costa and Colton will not have had any dealings with regard to Calpe.

112 The action is dismissed.

Judgment for the defendant.