Privy Council Appeal No. 38 of 1969

Tak Ming Company Limited – – – – – *Appellants*

v.

Yee Sang Metal Supplies Company – – – – *Respondents*

FROM

THE SUPREME COURT OF HONG KONG

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 5TH OCTOBER 1971

Present at the Hearing:
VISCOUNT DILHORNE
LORD SIMON OF GLAISDALE
LORD CROSS OF CHELSEA
[*Delivered by* LORD SIMON OF GLAISDALE]

This is an appeal from a judgment of the Supreme Court of Hong Kong in its appellate jurisdiction, dismissing an appeal from a judgment of the Supreme Court in its original jurisdiction, whereby the appellants were ordered to pay to the respondents such sum as should be awarded to them for the balance of the price of work done by them on a building site in excess of the sum of $884,000.00.

The respondents were the plaintiffs at first instance. They were sub-contractors for the steel and reinforced concrete work (compendiously called "the R.C.C.") on the building site. The first defendants in the action were the main contractors: they have taken no part in this appeal. The appellants, the second defendants in the action, were the owners and developers of the site.

The main contract between the appellants and the first defendants is dated 27th October 1964. It was a fixed price contract for the erection of a school for a price of $4,692,000.00. The schedule to the contract provided for the method of payment: subject to a retention fund of 25%, it provided for 41 payments against architect's certificates. Only the first 17 certificates and payments related to the successive completion of the R.C.C.; the 40th certificate and payment was on application for the occupation permit, and the 41st ($667,500.00) was on the issue of the occupation permit. The balance of the retention fund of 25% was to be paid within 30 days of the issue of the occupation permit. It is sufficient to summarise, without going into detail, by saying that the contract involved the first defendants in themselves to a substantial degree providing finance for the project.

On 20th January 1965 the first defendants (the main contractors) entered into a sub-contract with the respondents for the R.C.C. The respondents were to receive $100,000.00 on completion of certain steel work in the foundations; thereafter they were to get 10 payments of $50,000.00 and 10 of $45,000.00. Those last 20 payments were related to and were to be paid out of the first 20 payments due to the first defendants under the main contract; so that although the respondents would complete the R.C.C. by the time the 17th certificate was issued under the main contract, they would not fully receive all the fixed payments under the sub-contract till the issue of the 20th certificate under the main contract. It was stipulated that the payments to the respondents (other than the $100,000.00) were to be made direct to the respondents by the appellants' solicitors. There was to be a final adjustment of the sub-contract price according to the finally ascertained weight of the steel rods supplied by the respondents. The sub-contract of 20th January 1965 involved the respondents in financing to some extent the work on the sub-contract, though to a considerably less extent than the similar obligation on the first defendants under the main contract.

By the beginning of February 1965 the first defendants were having difficulty in performing their obligations under the main contract and it was envisaged that they might default, involving the appellants in placing the contract elsewhere. The appellants were, however, anxious in such an event to retain the respondents as contractors for the R.C.C.— at least partly, it may be surmised, because they were in effect a source of finance. In consequence a meeting took place between representatives of the appellants and the respondents. The upshot was an exchange of letters dated 5th February 1965 and 9th February 1965. Their Lordships do not think it necessary to set out the terms of the letter of 5th February; because if it was an offer it evoked not an acceptance but a counter-offer. But the letter of 9th February 1965 from the appellants to the respondents must be set out in full:

" Dear Sirs,

Re: Tak Ming Middle School at
K.I.L. 1571, S.A., 76, Sai Yee Street, Kowloon

We acknowledge receipt of your letter of 5th February, 1965 and we wish to confirm to you as follows:

(1) In case of the breach of contract No. 574 dated 27th October, 1964 from the part of Messrs. Defag Construction Co. [the first defendants] we may by mutual agreement between your goodselves and ourselves continue the contract signed on 20th January, 1965 by your goodselves with Defag Construction Co. even though the said contractor should be forced out of the above site.

(2) In case of the failure to reach a mutual agreement between us we shall pay you for the works done on the captioned site against our architect, Mr. Eric Cumine's certificates in accordance with the Building Contract No. 574 prepared and signed in the said architect's office.

The above confirmation is subject to your fulfilment of the terms of your contract with Defag Construction Co. mentioned in your letter of 5th February, 1965 addressed to us and also subject to your

carrying out works properly and expeditiously in accordance with the schedule of works submitted to the aforesaid architect and to us by the contractor, Messrs. Defag Construction Co.

Yours truly,

TAK MING CO., LTD. H.K.

(Sgd.) (Illegible)

Director."

The stipulated date for completion by the first defendants was successively postponed, with the resultant postponement of the completion date of the intermediate stages. The revised date for completion of the R.C.C. was 12th July 1966: on 5th July 1966 it was certified by the architect as having been completed by the respondents. On 3rd September 1966 the appellants gave notice to the first defendants of termination of the main contract on the ground that the first defendants were in breach. Apparently no other main contractor was appointed; but the building was completed shortly thereafter and an occupation permit issued. The respondents had done all the work that they had contracted to do under the sub-contract, save for a small item which they had been prevented from doing by the refusal of the appellants to allow them on the site for this purpose. The architect had issued certificates relating to all the payments under the schedule of the principal contract, except the 20th, 21st and 41st: the 20th and 21st did not relate to work to be done under the sub-contract, and the 41st related to the large sum payable on the issue of the occupation permit.

The respondents had been paid $884,000.00 through the appellants' solicitors. They claimed the balance alleged to be due to them ($367,645.75); and, on failing to obtain satisfaction, they issued a writ against the first defendants and the appellants. They signed judgment in default against the first defendants; but, the judgment remaining unsatisfied, they continued the action against the appellants. It was agreed that the issue of liability should be determined first. Pickering J. found in favour of the respondents, and his judgment was upheld on appeal.

Before their Lordships two main arguments were advanced on behalf of the appellants: first, there was no contractual nexus between the appellant and the respondents; and, secondly, if there was a contract, on its proper construction the appellants were only bound to make payments to the respondents on certification by the architect under the schedule to the main contract and the architect had certified some only of such payments—in particular, the crucial 41st payment was uncertified.

For their first contention the appellants relied on the well-established principle that a contract between a developer and a main contractor together with a related sub-contract between the main contractor and a sub-contractor does not create privity of contract between the developer and the sub-contractor. Their Lordships do not doubt this principle; but it does not preclude a developer and a sub-contractor establishing a contractual relationship independently of the main contract and the sub-contract. That is what was done in the instant case. Their Lordships agree with the view of the learned trial Judge and of the Full Court that the appellants' letter of 9th February 1965 amounted to an offer to the respondents, intended to create a contractual relationship, which was accepted by the respondents' performance. Indeed, this was the view of the appellants themselves: a letter from their solicitors dated 26th October 1966 contains the following passage:

> "Our clients inform us that they do not consider themselves bound to make any payment under their letter to your clients dated the 9th February 1965, by virtue of the fact that your clients failed to comply with the final paragraph of the above mentioned letter, in that they failed to carry out the work properly and expeditiously in accordance with the Schedule of Works submitted to Mr. Eric Cumine and to Tak Ming Company Ltd."

This proceeds on the assumption that the appellants and the respondents were in contractual relationship by reason of the letter of 9th February 1965, but claims that the appellants were exonerated from performance of their side of the bargain owing to the respondents having failed properly to perform their own.

If, then, there was privity of contract by reason of acceptance by performance on the part of the respondents of an offer made in the appellants' letter of 9th February 1965, what is the proper construction of the terms of that letter with regard to payment of the respondents by the appellants for work done in accordance with the sub-contract? The appellants contend that it means that they should only pay the respondents for work done against the architect's certificates issued in accordance with the main contract: the respondents have already received payment under the architect's certificates certifying payments due under numbers 1–17; and the architect had never thereafter issued any certificates certifying payment under any number relating to work done by the respondents. The respondents, on the other hand, contend that the letter imposed an obligation on the appellants to pay them the outstanding amounts certified by the architect as relating to work done by them. The construction contended for by the appellants seems to their Lordships to be an impossible one. Both extrinsically and from the terms of the letter itself it is apparent that the background against which the new relationship between the appellants and the respondents was created was the possibility that the first defendants would default on their obligations under the main contract. If they did so, no further certificates would be issued in their favour. It is absurd to suppose that the appellants and the respondents were agreeing that the respondents would in such circumstances be precluded from receiving payment for work they had done for the benefit of the appellants. Their Lordships agree with the construction of the learned trial judge and of the Full Court.

The respondents have done all the work they contracted to do under the sub-contract (save for a small item they were prevented from doing by the appellants). By their letter of 9th February 1965 the appellants agreed that if the respondents did such work the appellants would pay them for it in the event of default by the first defendants. The first defendants have defaulted. The appellants are therefore liable to the respondents for the balance, if any, of the price of the work done by the respondents on the appellants' site in excess of the sum of $884,000.00 already received by the respondents in respect thereof.

Their Lordships will therefore humbly advise Her Majesty that the appeal should be dismissed. The appellants must pay the costs.

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In the Privy Council

TAK MING COMPANY LIMITED

v.

YEE SANG METAL SUPPLIES COMPANY

DELIVERED BY
LORD SIMON OF GLAISDALE

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