Client Alert

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Salutary Lessons in DIFC Contract Law: Hexagon Holdings (Cayman) Limited v. DIFC Authority and DIFC Investments LLC (CFI-013-2019)

August 9, 2022

What this Article Discusses

Termination for fundamental breach under DIFC Contract Law – failure to give notice of termination within a reasonable time – whether a reservation of rights extends the time period for termination – affirmation – anticipatory breach – agreements to agree - the importance of cross-examining on all material issues.

Introduction

On 4 August 2022, Justice Robert French, sitting in the DIFC Court of Appeal, dismissed an application by the Claimant, Hexagon Holdings (Cayman) Limited ("Hexagon"), for permission to appeal against the Judgment of Justice Sir Jeremy Cooke dated 2 March 2022, which had dismissed Hexagon's claims in full. So ended one of the largest damages claims to reach full trial in the DIFC Courts, with a combined claim value of US $500 million.

The trial was the culmination of a 16-year saga between Hexagon and the DIFC Authority and its subsidiary, DIFC Investments (together, the "Defendants"), regarding a failed joint venture to develop land in the Dubai International Financial Centre (the "DIFC"). In the end, after three years of hard-fought litigation (including an initial strike-out of Hexagon's claim), Hexagon's claim proved to be entirely unmeritorious, with the Defendants winning on every material issue at trial. Akin Gump[1] (Graham Lovett, Michael Stewart and Sophia Cafoor-Camps) and Tom Montagu-Smith QC acted for the Defendants.

The case involved a number of interesting legal issues stemming from the peculiar facts: Hexagon claimed that between 2006 and 2012, the Defendants had breached a joint venture agreement and had also renounced the same agreement in 2012, and yet Hexagon did not purport to terminate until 2018. The Court heard arguments regarding agreements to agree, withdrawal of renunciation, loss of the right to terminate under DIFC Contract Law for failure to give timely notice, and common law affirmation. The case also serves as a salutary reminder for practitioners that the DIFC Court requires witnesses to be challenged in cross-examination on all material points in dispute.

Contact Information

If you have any queries regarding the alert, or disputes more broadly, the experienced team at Akin Gump is on hand to assist:

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The Claim

The claim related to a DIFC law governed joint venture agreement entered into in 2003 and amended in 2004 (the "AJVA"). In the AJVA, the parties agreed to take various steps to establish a joint venture company which would develop what is now one of the last undeveloped plots of land in the DIFC. The steps included: (i) the execution of a shareholders' agreement which, critically, was to reflect the terms of the AJVA, including the terms as to how the project would be funded; (ii) the incorporation of a joint venture company (the "JVCo"); and (iii) the transfer of the land to the JVCo. The parties agreed to use best endeavours in good faith to achieve those steps as soon as reasonably practicable.

Hexagon alleged that the Defendants had breached those obligations between 2006 and 2012. The case finally put at trial was that Defendants had never really intended to proceed with the joint venture and had engaged in the pretence of negotiations.

The six-year statutory limitation period under DIFC Contract Law for breach of contract meant that only an alleged breach in 2012 was in time. Hexagon purported to terminate in late 2018. Hexagon's case was that in the six-year period between the in-time breach and purported termination, the parties had engaged in settlement negotiations to resolve the dispute, during which time it validly reserved its termination right. When those negotiations finally broke down in late 2018, Hexagon had therefore validly elected to terminate.

There was also a separate claim that the Defendants renounced the AJVA in 2012. The Defendants accepted that they had sent a letter in 2012 stating that the AJVA was no longer binding due to various factors (the "2012 Renunciation"). However, subsequently the Defendants had reconsidered their position and unequivocally recommitted to the joint venture, and all negotiations from then onwards proceeding on that footing. In 2018, when the negotiations broke down, the Defendants had even issued a notice expressly requiring that the parties proceed in accordance with the terms of the AJVA. The Defendants argued that any renunciation was therefore withdrawn as at the date of the purported termination.

Key Issues

The key issues in dispute were:

1. Did the Defendants breach the obligation to use their best endeavours in good faith to negotiate a shareholders' agreement?
2. Did the Defendants withdraw the 2012 Renunciation, such that it was not clear that there would be fundamental non-performance at the date of termination in 2018 (as required by Article 88 of the DIFC Contract Law for termination for anticipatory breach)?
3. If there was a breach:
    a. Was it in time?
    b. Did Hexagon terminate within a reasonable time, as required by Article 87(2) of the DIFC Contract Law?
    c. Alternatively, did Hexagon affirm the AJVA at common law?
    d. Would Hexagon have performed but for the breach?

e. If there was a breach and/or renunciation and termination was valid, had Hexagon suffered any loss of profits, or alternatively reliance loss?

The Judgement

Justice Sir Jeremy Cooke comprehensively found for the Defendants on all the above issues, issuing his 106-page judgment a week after the trial finished.

1. Breach of the AJVA

On a proper construction of the AJVA, the Judge found that the obligation to use best endeavours in good faith to agree a shareholders' agreement did not require a party to vary the terms of the AJVA. The AJVA said the shareholders' agreement had to comply with its terms, which in particular obliged Hexagon to fund the development via 'liquid finance' – i.e. cash. There was no obligation to agree something contrary to those financing terms (or indeed other project details specified in the AJVA). The Judge's interpretation of the AJVA was supported by the fact that any alleged obligation to reach agreement beyond the terms of the AJVA would be an agreement to agree, lacking an objective yardstick to adjudge the parties' conduct and thus uncertain and unenforceable.

His Honour found that Hexagon had sought to depart from the terms of the AJVA from 2006 onwards, by proposing alternative terms that limited (and eventually entirely removed) the cash investment obligation. There was no breach by the Defendants in failing to agree to those proposals. Contrary to Hexagon's fanciful conspiracy theory that the Defendants were never committed to the joint venture, the Judge also found that the Defendants acted in good faith at all times and had made concessions in the negotiations which they had no obligation to make.

The Judge further found that:

1. The allegations of breach of contract were all statute barred;
2. Any right to terminate would in any event have been lost for two reasons:
    a. First, Hexagon failed to exercise its termination right within a reasonable time, as required by DIFC Contract Law. The Judge said that a party could not retain a right to terminate over a period in excess of six years.
    b. Second, Hexagon had affirmed the AJVA as a matter of common law. Whether there has been an affirmation is a multifactorial assessment. The Judge found that affirmation had occurred due to: (i) the passage of time, and (ii) Hexagon's post breach conduct, which was consistent with the existence of the AJVA.

The fact that Hexagon made sporadic reservations of rights in correspondence was not enough to prevent an affirmation in the circumstances. This aligns with recent Court of Appeal authority in England & Wales[2], which held that, while a reservation of rights will often have the effect of preventing subsequent conduct constituting an election, that is not an invariable rule, and a finding of election depends on the totality of the circumstances. There may come a time when delay in exercising a right will be of such a duration that, notwithstanding a reservation of rights, a party will be held to have affirmed.

One point of interest is that the Judge found both a failure to exercise a termination right within a reasonable time under DIFC Contract Law, and affirmation as a matter of

the common law of England & Wales. This suggests that the DIFC Contract Law is not a complete code, and co-exists with the common law of contracts, although this issue was not directly argued before the Court. This is an important question that will need to be answered in due course.

2. Renunciation of the AJVA

The renunciation claim was also dismissed by the Judge on the basis that the Defendants had recommitted to the AJVA following the 2012 Renunciation and would have performed its terms. Hexagon could not rely on Article 88 of the DIFC Contract Law (termination for anticipatory non-performance), which requires that it be clear that there will be fundamental non-performance at the time of termination. This is a useful reminder that an anticipatory breach is a thing 'writ in water', and a party who fails to make an election will lose a termination right where the non-performing party resumes performance.

3. Causation

Hexagon's witness admitted in cross-examination that after the Global Financial Crisis it was not "foreseeable" that the Claimant would proceed on the original financing terms (i.e. 100 percent cash funding). Further, the evidence produced regarding Hexagon's ability to fund the development in cash was vastly inadequate and Hexagon had failed to comply with a document production order as to its willingness and ability to fund, leading to the Judge drawing adverse inferences. The Judge therefore found that Hexagon would not have proceeded with the AJVA in any event. As no project would have occurred, the alleged breaches – even if they did occur – did not cause any loss.

4. Quantum

The Judge also preferred the Defendants' evidence on quantum, concluding that Hexagon's expert "*was wrong on nearly [all] the issues that mattered*". The key point of difference between the experts was discounting. Hexagon's expert did not perform a discounted cash flow analysis, whereby a discount rate based on risk and accelerated receipt is applied to forecast profits. This was contrary to standard practice for valuations of this nature, according to the Defendants' expert. The Judge agreed, finding that the reasons given by Hexagon's expert for not applying discounting "*made no sense*".

The Defendants' expert's evidence was that the proposed project would not have been profitable for Hexagon once cash flows were discounted, even if all of Hexagon's other assumptions were accepted. If this was accepted by the Judge, it was fatal to the quantum claim. Curiously, the Defendants' expert was not cross-examined on the issue, and indeed on the vast majority of the critical points of difference between the experts. Instead, the Defendants' expert was largely cross-examined on his integrity, with the apparent intention being to try to impugn his overall evidence based on alleged impartiality. The Judge found this approach to have been "*utterly misplaced*" and make a number of pointed criticisms of the Claimant's conduct in closing. The result was that the Court was bound to accept the Defendants' evidence on unchallenged matters, including discounting, unless it was utterly incoherent. The Judge noted that he would have done so anyway, following cross-examination of Hexagon's expert.

This is a further demonstration from the DIFC Court that the standard and robustness of advocacy is high and the traditional rules of evidence will be strictly applied. Unlike in the international arbitration space, where tribunals sometimes take a more informal approach to evidence, failure to challenge witnesses can result in the DIFC Court's hands being tied as to the acceptance of that evidence, and have significant ramifications for the case.

Permission to Appeal

Hexagon first applied for permission to appeal to Justice Cooke. The grounds of appeal failed to challenge the Judge's findings regarding breach, time bar and causation, meaning the application was doomed from the outset. The balance of the grounds raised were either a gross distortion of the Judgment or impermissible factual challenges based on a 'cherry picking' of the evidence. The Judge ultimately found that Hexagon's case was "*in part incoherent and in whole unmeritorious*", and that, coupled with the flawed nature of the appeal, meant there was no real prospect of success. Hexagon's application for permission to appeal was therefore dismissed with indemnity costs.

Hexagon's further application for permission to appeal to the Court of Appeal suffered from the same defects and met with the same fate, with Justice Robert French dismissing Hexagon's application, again with indemnity costs.

Conclusion

Ultimately, the Defendants were fully vindicated. Hexagon's baseless insinuations that the Defendants had 'dragged their heels' and failed to negotiate in good faith were resoundingly rejected on the evidence. To the contrary, they were found to have acted in good faith at all times.

For commercial parties, there are several lessons:

1. First and foremost is that, when a right to terminate is thought to arise, the electing party should act promptly and decisively. The law grants a limited grace period within which to make a decision. Take too long and you may be taken to have affirmed (or in DIFC Contract Law parlance, the reasonable time period for termination will expire). In the case of anticipatory breach, there is also the risk that the other party will resume performance.
2. Express reservations of rights and without prejudice correspondence are useful tools to extend your right to make an election, so long all communications unequivocally proceed on that basis. Even then, the Courts of England & Wales, and now the DIFC Courts, recognise that the passage of time may overwhelm a reservation.
3. Failure to engage with Court Orders for disclosure may well result in the drawing of adverse inferences which may ultimately be fatal to a claim or defence regardless of other factors.
4. Alleging dishonesty is easy to do but often very hard to evidence – particularly in the course of commercial negotiations where each party is acting in its own best interests. If you are going to allege dishonesty, you need to make sure that you can prove it, or the Court is likely to take a dim view of your claims.

[1] The trial occurred while the team was at Gibson, Dunn & Crutcher.

[2] *SK Shipping Europe Limited v Capital VLCC 3 Corp & Anor* [2022] EWCA Civ 231