Neutral Citation Number: [2019] EWHC 2310 (TCC)

Case No: HT-2019-00067

IN THE HIGH COURT OF JUSTICE
BUSINESS AND PROPERTY COURTS OF ENGLAND AND WALES
TECHNOLOGY AND CONTRUCTION LIST (QBD)

Royal Courts of Justice, Rolls Building
Fetter Lane, London, EC4A 1NL

Date: 05/09/2019

Before :

HIS HONOUR JUDGE BIRD
(Sitting as a Judge of the High Court)

- -

Between :

SURGO CONSTRUCTION LIMITED	**Claimant**
- and -	
PLANET BIOGASTECHNIK GMBH	**Defendant**

- -
- -

Mr William Webb (instructed by **DAC Beachcroft**) for the **Claimant**
Mr Gideon Scott Holland (instructed by **Fieldfisher**) for the **Defendant**

Hearing dates: 12 July 2019

- -

Approved Judgment

.....

His Honour Judge Bird QC :

The Claim

1. Between July 2013 and October 2015 Surgo Construction Limited ("Surgo") engaged PlanEt Biogastechnik GmBH ("PlanEt") under separate contracts to complete certain works comprising the supply and installation of anaerobic digestor power plants at 5 sites: Ponsonby, Howla Hey, Wray House, Gravel Pit and Hope House. During the course of the works, PlanEt mistakenly charged VAT to Surgo in the sum of £1,177,478.12 which sum Surgo paid. The mistake was discovered in 2016.

2. The parties agree that the mistake arose because PlanEt (as a German registered company) had no right to charge the VAT to Surgo. VAT was correctly due on the relevant supplies, but ought to have been paid by Surgo directly to HMRC. Surgo remains under a liability to pay the sum of £1,177,478.12 to HMRC.

3. PlanEt, having wrongly charged Surgo and having wrongly received the VAT, accounted for it to HMRC. In light of the mistake as to the mode of collection, PlanEt became entitled to reclaim the VAT they had paid to HMRC. They have recovered, by way of payment or credit against other tax liabilities, £1,226,014.21 and accept that that sum should, as an accounting exercise at least, be treated as a credit to the account of dealings between it and Surgo. It has agreed that this treatment should result in a repayment of £77,029.47 but seeks to retain the remainder on the basis that it is owed to it by Surgo.

The Proceedings

4. Surgo commenced proceedings on 26 February 2019 claiming repayment of the VAT it paid either on a restitutionary basis or on the basis of an implied term of the contracts. Giving credit for the £77,029.47 paid, the sum claimed is £1,100,448.65. On 9 May 2019 Surgo issued an application for summary judgment. This is the hearing of that application.

5. The principles on which I should proceed were not in issue. The test for summary judgment is well known.
6. The key question for determination is whether PlanEt is entitled to withhold repayment and if so on what basis?

The Claimed Rights to withhold repayment (the facts)

7. PlanEt submits that it has at least a reasonable prospect of successfully defending the claim at trial so that the application for summary judgment should be dismissed. Factually it relies on the following evidence set out in the witness statement of Eleanor Pinnells filed in opposition to the application to support a set off argument. PlanEt's argument is based on the assertion that these claims have sufficient prospects of success, in themselves, to defeat a claim for summary judgment:

    a. The claims relate only to the Gravel Pit and Hope House contracts.

    b. In respect of Gravel Pit it is said that £859,457.60 is owed to PlanEt by reason of:

        i. a Take Over dispute which has led to the holding back of retentions in the sum of £260,315.14. PlanEt's evidence is that it had met the relevant Take Over standards by the end of April 2017 so that Surgo ought to have certified Acceptance by mid-May 2017. The certificate of Acceptance would trigger the release of the retentions.

        ii. the costs of additional work in the sum of around £39,000.

        iii. an increase in the cost of servicing a performance bond provided under the terms of the contract. The certificate of Acceptance should (say PlanEt) have resulted in the cancellation of the Bond. The Bond incurs a monthly servicing fee of £1,094.50. The total claim at the date of PlanEt's evidence, was for £34,364.33. The Bond itself was procured in the sum of £535,615.46 and is payable on written demand by Surgo and will expire once the certificate of Acceptance is issued.

        iv. the principal bond sum of £535,615.46. The bond was provided on 6 July 2016 in accordance with the obligations set out at schedule 23 of the contract for 15% of the subcontract price and was to be valid until the issue of certificate of Acceptance. The costs of the Bond were to be met by the Contractor. The basis of the claim for the principal bond sum is set out at paragraphs 65 to 72 of PlanEt's evidence. In short the argument is that PlanEt "is at real risk of Surgo claiming for the full amount under the Bond at any

time without needing to show cause".

c. In respect of Hope House, £242,715.76 is owed by reason of a Takeover dispute. PlanEt's evidence is that it met the relevant standards by the end of March 2017 so that Surgo ought to have certified Acceptance (so releasing the retentions) by early April 2017.

8. The Takeover disputes (and the consequent apparent failures to issues certificates of Acceptance) represent the largest element of PlanEt's claims. PlanEt does not suggest that at this early stage of the proceedings it is possible to explore the merits of the claims in anything other than a relatively superficial way. It does however suggest that each passes the summary judgment test and in respect of the Gravel Pit contract, the purchaser has certified Takeover to Surgo and has been operating the plant for 2 years or more.

The Claimed Rights to Repayment (the law)

9. Against that factual background, PlanEt identifies its claim to retain the benefit of the VAT monies paid as arising either under an equitable set-off or a statutory (or legal) set off.

10. The law in respect of equitable set-off finds its most recent and authoritative explanation in the Court of Appeal's decision in *Geldoff Metaalconstructie NV v Simon Carves Limited* [2011] 1 Lloyd's Rep 517. At paragraph 43 of the unanimous judgment, the Court sets out 6 principles that can be drawn from the earlier cases. The relevant points (which were not in any real dispute before me) are:

a. There is a "formal requirement" of close connection between the claims to be set-off one against the other. The necessary connection between the claim and the cross claim has been described in different ways and the Court of Appeal repeated a long-standing warning derived from earlier cases not to "get caught up in the nuances of different formulations".

b. There is a "functional requirement" that it must be unjust to enforce the claim whilst ignoring the cross-claim.

c. A two-stage test should not be applied. Rather the formal and functional requirements should be considered as part of one question: the formal requirement emphasises that

equitable set-off is based in principle not discretion, and the functional requirement is a reminder that the ultimate basis of the remedy is equity.

d. The single test to identify a cross claim that is an equitable set-off is best expressed as a claim "…so closely connected with the [Claimant's] demands that it would be manifestly unjust to allow him to enforce payment without taking into account the cross-claim".

11. The law in respect of legal set off is again well established. I take the statements of principle at paragraph 36, 37 and 39 of Mr Scott Holland's skeleton argument (for PlanEt) to be accurate. For there to be a legal set-off:

a. Both parties must owe each other a debt (either of a liquidated sum or in a sum which is capable of ascertainment without valuation or estimation) If a valuation or an estimation is required, the debts are not sufficiently certain – they must be ascertainable "readily" and "without difficulty" (*Aektra v Exmar* [1994] 1 WLR 1634)

b. The debts must be mutual (that is the parties must be the same and must be acting in the same capacity)

c. The debts must be due and payable.

12. There is little law on the question of whether set off can be raised against a claim for restitution.

13. As to equitable set-off, Mr Webb (for Surgo) has drawn my attention to the case of *Fenice Investments Inc. v Jerram Falkus Construction Limited* [2010] EWHC 1662 (TCC). The judgment concerned an application for summary judgment in respect of a sum of money paid by the Claimant under a mistake of fact (the mistake being that the payment had not already been paid. In fact it had). The Defendant raised an arguable cross-claim as a set-off. At paragraph 22 of the judgment Ramsey J accepted that the cross-claim was arguable. At paragraph 24 the Judge sets out the question he was to deal with: can the arguable cross-claim he has just identified be advanced as a defence to a restitutionary claim? At paragraph 24 he noted the absence of any reported decision on the point.

14. At paragraph 25 he refers to a situation where the party claiming restitution holds money which must be taken into account in deciding the extent of the unjust enrichment. Ramsey J then referred to *Westdeutsche Landesbank v Islington BC* [1994] 4 All ER 890 at first instance and reference within the judgment to the earlier case of *Hicks v Hicks* (1802) 3 East 16.

15. I was not taken to Hicks, but the facts of the case appear from the report (and from the *Westdeutsche* report in the Court of Appeal). The claimant had purchased an annuity from the defendant. Sums were paid to the claimant under the annuity for a number of years. The annuity was found to be void for want of registration. The claimant brought an action to recover the price he had paid for the annuity. The defendant was held entitled to set-off sums paid under the annuity against that claim. Lord Ellenborough felt that the money paid for the annuity and the money received under it were both "money had and received". The principle was applied (see the Court of Appeal judgment) by Sir William Grant M.R. in *Holbrook v. Sharpey* (1812) 19 Ves.Jun. 131 . Grant M.R. also said, at p. 132:

> *"Either all the payments, made under a void annuity deed, must be considered as purely voluntary, in which case none of them could be recovered back: or they are all money had and received to the use of the grantor, and therefore to be all returned or accounted for."*

16. Returning to *Fenice*, Ramsey J held (at paragraph 26) that where there was a claim for repayment of liquidated damages the *Westdeutsche* type of set off did not apply. He said the claim before him "was not equivalent to the position where there is a claim for the balance of money held by the two parties".

17. Ramsey J went on to hold that the general principles of equitable set-off apply to a restitutionary claim, but that there was no sufficiently close connection in the case before him to allow a set off. He concluded that it would be manifestly unjust to allow an equitable set-off.

18. In respect of legal set-off, *Fuller v Happy Shopper* [2001] 1 WLR 1681 suggests that such a set off is available. In that case the Claimant tenant claimed that rental payments should have been reduced under the terms of the lease by £2,092.50 per quarter. He continued to pay that sum and in later proceedings asserted that this was an overpayment made under a mistake of fact or law in respect of which he had a restitutionary claim. He sought to set off those overpayments against unpaid rent in proceedings for possession. The principle that legal set-

off was available was conceded and the concession recorded by the Judge (on appeal) without adverse comment. The concession then (by reference to the definition of legal set-off set out above) must have included (and been accepted as) a concession that the restitutionary claim was to be treated as giving rise to a "debt".

19. Insofar as the claim is based in contract there is (subject to the terms of the relevant contracts) no question that the set-off would, if established at trial, amount to a defence.

The Claimant's Response

20. In response to these points, Surgo argues that there can be no set-off. It relies on clause 41.14 of the Gravel Pit and Hope House contracts as a contractual exclusion of set off rights. The relevant clause provides as follows:

> *"the Contractor [Surgo] may deduct and set off against any amounts due from the contractor to the subcontractor [PlanEt] under the subcontract. Save where expressly stated to the contrary, the subcontractor shall not be entitled to set off any amount due to the contractor by it"*

21. Something appears to have gone wrong with the drafting of the clause. If read literally the provision does nothing to prevent the subcontractor claiming a set-off against a debt due to the contractor. It may be (in order for the words chosen by the parties to have any meaning at all) that the provision should be read as applying to prevent a set-off by the subcontractor of any sums due to it by the contractor.

22. At this, very early stage of the proceedings, bearing in mind that the point was first raised in argument and is not dealt with in the evidence, it seems to me that it would be wrong to speculate on how the Court at trial might interpret the provision or what the prospects of success would be in respect of an (as yet unpleaded) claim for rectification. For the purposes of determining the present application it seems to me that I should not take the provision as prohibiting set-off in the Hope House and Gravel Pit contracts. However read, the term has no application to the other contracts.

23. Surgo submits that no equitable set-off is available. It makes the following points:

a. At best, an equitable set-off could only be raised in respect of sums due on the Gravel Pit and Hope House contracts. The contended for cross claims arise only under those contracts. As far as the Surgo's claims under the other contract are concerned: there is very little connection between the cross claims arising under the Hope House and Gravel contracts and the claim under the Ponsonby, Howla Hey and Wray House contracts. It would not be manifestly unjust to allow Surgo to claim back the VAT paid on those contracts without taking into account the cross-claims.

b. Insofar as the claim is a claim for restitution, if any right to equitable set off arises at all, the mere fact that the claim and cross claim arise under the same contract is insufficient to satisfy the formal requirement of close connection. This is the effect of the *Fenice* decision. Further and in any event, the functional requirement of injustice is not met.

24. As far as the legal set off is concerned Surgo submits none is available:

a. Insofar as the claim is based in restitution it is not a debt claim and so there can be no legal set-off. This again appears to be the effect of the *Fenice* decision, where there appeared to be mutuality of debts.

b. Insofar as the claim is based in contract the cross claims on any view are not due and payable because the contractual formalities of demand or issuance of certificates have not been met and the claims in respect of additional works and of servicing the bond are not liquidated.

25. Surgo also submits that the sums it paid by way of VAT were appropriated by it to payment of VAT. It is not now open to PlanEt to appropriate the payments elsewhere. Surgo relies on *Thomas v Ken Thomas* [2006] EWCA Civ 1504. The key points to be derived from the decision are set out at paragraph 18 of Mr Webb's skeleton:

a. A debtor may choose what debt a payment is appropriated to. Here, Surgo paid sums over to PlanEt which each included a readily ascertainable amount of VAT (one-sixth of the total paid[1]). There was an appropriation therefore of one-sixth of each sum paid to VAT. The appropriation was, in essence, mutually agreed upon because it was

[1] If Surgo paid £100 + VAT in the total sum of £120, 1/6 of the £120, ie £20, is the VAT element of the claim. This is known as "the VAT fraction" and is applied to net down a VAT inclusive payment

invoiced by PlanEt.

b. The debtor's appropriation cannot be challenged by the creditor and the creditor cannot simply shift the payment to another debt. The point is all the stronger where appropriation was mutual.

c. If the creditor does not agree with the debtor's appropriation its remedy is to refuse to accept the money and return it.

26. Surgo submits that there is no basis to the claim for the value of the bond.

Discussion

27. I should deal first with some short preliminary matters, considering short arguments advanced during the course of the hearing:

a. PlanEt raised a brief argument that any unjust enrichment had not been at the expense of Surgo, because Surgo had suffered no loss and so argued that there should be no summary judgment on that part of the claim. I accept that there is nothing in the point; it is enough for Surgo to show that a benefit (here, a payment) has moved from it to PlanEt (see Goff and Jones at paragraphs 1-09 to 1-17 in particular at 1-17). The law of unjust enrichment is concerned with the reversal of transfers of benefits between claimants and defendants, not with disgorgement of gains or with compensation for loss suffered.

b. I am also satisfied that the proper quantification of Surgo's contractual claim is the sum it paid to PlanEt (after allowance is given for the sum repaid). The need for Surgo to account for that sum to HMRC is a matter of law and as I understand it is
c. not, in reality, disputed. In my view Surgo has suffered a loss and need not wait until the sums are actually paid over to HMRC before it is entitled to damages in contract. To hold otherwise would be to treat the claim as, in effect, a claim for an indemnity.

28. The issue of set-off against a restitutionary claim is an important question.

29. *Hicks*, which formed the foundation of the decision in *Fenice* involved payments made by claimant and defendant (received by the defendant and claimant) under a void instrument.

Each party would have a restitutionary claim based on payments he had made relying in each case on the same void instrument. The connection between the claims could hardly have been closer; they arose under the same instrument and in each case because the instrument was void each was a restitutionary claim. Justice clearly required that one claim should be set off against the other.

30. As to the availability of a legal set-off against a restitutionary claim, ***Happy Shopper*** seems to support the proposition that a restitutionary claim may be set-off (by way of legal set-off) against a debt.

31. In my view PlanEt's claim to an equitable set-off is weak and has no reasonable prospect of success. I am satisfied that the claims for losses suffered by PlanEt as a result of Surgo's apparent failure to comply with procedures laid down in the contract are not so closely connected with Surgo's claim for the repayment of money demanded as VAT that was not due as to raise anything like a "manifest injustice" sufficient to prevent the repayment of the sums paid as VAT.

32. The claims raised in respect of legal set-off are, in part, different. In my view, for the purposes of the summary judgment application in respect of the claim in contract, there is a reasonable prospect of success in establishing at trial that the sums of £260,315.14 and £242,715.76 are capable of being set off against the sum claimed. Each of these sums is liquidated or ascertainable because the sum comprises retentions. These debts, when compared to the claim for the repayment of the sums wrongly paid by way of VAT are mutual debts and in my view, there is a reasonable prospect that the Court will find that such sums are due and payable. I am also satisfied that the cost of servicing the bond, fixed as the date of PlanEt's evidence at £34,364.33 is a liquidated sum, that there is mutuality and that there is a reasonable prospect at trial of the court finding that the sum is due.

33. I am not satisfied that the claims for additional works and the principal sum of the bond are due. The claim for the latter is based on a continued exposure to the risk of the bond being called on. The claim for the full value of the Bond in my view has no reasonable prospect of success at trial and indeed it is difficult to follow. If the Court finds that the certificate of Acceptance should have been issued or should be issued, the Bond will be cancelled. The claim for additional works is in my judgment vague and at this stage nothing other than an assertion. The claim is small and was not pursued with vigour.

34. Given the decision in ***Happy Shopper*** it would in my judgment be wrong to conclude that the sums referred to above could not be set off (as a matter of principle) against the restitutionary claim.

35. I am not persuaded that the appropriation argument adds anything. At the time of payment both payee and payor intended that the sum should be allocated to pay VAT. The basis of that allocation involved a common mistake, namely that VAT was due. Once the mistake has been recognised, for the reasons I have set out, I am satisfied that an arguable case in respect of set off arises. To require the money to be repaid by reason of the initial and mistaken allocation would be to ignore set-off altogether. I am not satisfied that would be the correct course.

36. The effect of this judgment is that save for the sum of £537,395.23 (comprising £260,315.14; £34,364.33 and £242,715.76) there should be judgment for the Claimant. Judgment will therefore be entered in the sum of £563,053.42.