HFW

CONSTRUCTION BULLETIN
MARCH 2018

Welcome to the March edition of our Construction Bulletin.

In this edition we cover a broad range of recent contractual and legal issues relevant to the construction industry, as follows:

- Subcontracts Writ Large
- Is PPP feasible in the GCC?
- Qatar Crisis and Force Majeure
- Australian High Court Limits Grounds for Judicial Review of Adjudication Determinations

The inside back page of this bulletin contains a listing of the events at which the members of the construction team will be speaking over the upcoming months.

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Subcontracts Writ Large

One of the effects of the Carillion collapse was to focus a light on contractual arrangements throughout the construction supply chain, and the impact on parties when things go wrong. Over the years, much has been done in the UK to try and protect subcontractors, such as the Construction Act's prohibition on pay-when-paid clauses and introduction of statutory adjudication, and the current UK government's consultation on retention payments. Yet recent events have taught us there is more to be done. It is fundamental to ensure that risk is appropriately allocated throughout the supply chain by putting in place effective and properly drafted subcontracts.

In this article I offer some guidance on how main contract requirements should be addressed when drafting and negotiating subcontracts.

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Standard Form Subcontracts

The most straightforward scenario is where standard forms are used. NEC, FIDIC, IChemE and JCT, for example, all produce forms of subcontract designed to be largely back-to-back with main contracts of the same suite. Using standard forms in this way provides consistency of processes throughout the supply chain. Care always needs to be taken to ensure that any bespoke amendments to the standard form are also stepped down as appropriate.

Stepped-Down Bespoke Subcontracts

On large scale projects involving EPC-type contracts, it may be appropriate to use bespoke subcontracts for any major packages of works, flowing down relevant provisions from the main contract. Where the Construction Act applies, it is important to avoid conditional payment clauses. If the Act does not apply, any equivalent project relief clauses should be accompanied by effective name borrowing provisions.

Simple Back-To-Back Agreements

It might be tempting to try and short-cut matters by incorporating the entire main contract into a subcontract, using wording such as, *"The terms and conditions of the Main Contract shall apply mutatis mutandis to this Subcontract"* or *"The Subcontractor accepts the obligations of the Contractor under the Main Contract".*

This is obviously a quicker approach to drafting. However, save in limited circumstances, it is not an appropriate way to proceed. At the very least, it creates uncertainty between the parties as to which terms apply and how main contract terms are to be modified. Further, there will be provisions in the main contract which will be inapplicable to subcontracts.

Acknowledgement of Main Contract Provisions

Where main contract provisions are applicable to a subcontract, for example, access to site, performance specifications, FOI or bribery and corruption, it is good practice for the relevant clauses to be set out in full; either in the body of the subcontract, or as a schedule, with a requirement for the subcontractor to comply with such provisions.

Otherwise, it may be sufficient for the subcontract to require the subcontractor to carry out the subcontract works in such a manner as not to put the contractor in breach of the main contract. When signing up to such a provision, it is essential that subcontractors are provided with copies of main contract documents, and read and understand them!

Conclusion

In practice, drafting and negotiating subcontracts is not given the same amount of attention as main contracts. Yet, as subcontractors are often the ones carrying out much of the work, this should not be overlooked. Getting subcontracts right can do a lot to manage the risk of project failure – or success.

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Is PPP feasible in the GCC?

PPPs have been successfully implemented across a range of projects globally, such as hospitals, power facilities, roads and airports. That success, combined with the pressures of growing populations, a corresponding need for infrastructure and falling oil prices, make PPPs an attractive model for GCC government procurement.

What is PPP?

PPP (Public Private Partnerships) broadly describe contracts between the private sector and public sector for the purpose of developing public assets or providing public services. The private sector will commonly provide the capital investment for the project and then recovers this investment, expenses and profit under contracts spanning several years from revenues generated by the asset or service. In return, the private sector will bear most of the risk and management responsibility. The public sector may then take over running the asset or service itself, bearing only the on-going operating expenses.

Advantages of PPP

The key benefit for governments is that they receive new, often much-needed development, without the associated capital investment. In addition, they can take advantage of private sector skills and expertise and transfer project risk to the private sector. PPP projects are usually infrastructure or services with a high chance of income-generation and the private sector gains access to these major, revenue-generating assets with government backing.

A cure-all?

Though attractive, PPP is not a panacea. Key concerns include:

- **Project viability:** Not every project is appropriate for PPP. Low-income assets are unlikely to attract private investment without guaranteed minimum revenues.
- **Certainty and security:** The more certainty a government can offer, the lower the private sector's risks will be. Key to this are legislative, regulatory and judicial frameworks that provide certainty and security for investors.
- **Customer intelligence:** The public sector must ensure that the asset or service can be delivered to the required standard, requiring an experienced supervisory team to step-in if necessary.
- **Privatised profit, socialised risk:** The private sector's duty to maximise profits can lead to cost-cutting and inferior quality. Governments (and ultimately the public) can be left picking up the tab if the private sector abandons the project.

PPP in the GCC

PPP is the current buzzword across the GCC, with an increasing desire for procurement using this model. Progress varies between states:

- Kuwait first introduced a PPP law in 2008 (updated in 2014) and has announced an ambitious programme of PPP projects, supervised by a dedicated PPP authority – the Kuwait Authority for Partnership Projects.
- Bahrain also adopted PPP early on, with the first project for affordable housing signed in 2012.
- In the UAE a number of PPP projects have been procured. Dubai introduced its own PPP law in 2015, while in 2017 the UAE's Federal Ministry of Finance published a PPP manual.
- Saudi Arabia has no dedicated PPP law, but has nevertheless embraced PPP. Ambitious development plans include privatisation of several of the nation's airports as part of its "Vision 2030".
- Oman has declared plans for US$2 billion of PPP projects and plans to introduce a PPP law
- Qatar implemented its first true PPP project in 2015 and has a dedicated PPP law on the way.

Despite this variance, we expect PPPs to become significantly more prevalent as the PPP framework matures across the market, with the success of PPP projects across the region followed with interest.

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Qatar Crisis and Force Majeure

We consider the force majeure provisions under the 1999 FIDIC Red and Yellow Book contracts (the FIDIC Contracts), along with some of the pitfalls contractors should consider when contemplating such claims.

Introduction

Force majeure has been a hot topic recently: last year, a diplomatic crisis between Qatar and its neighbouring Gulf States (the Qatar Restrictions) caused shockwaves throughout the region. Diplomatic ties were cut, with many of Qatar's neighbours closing or restricting borders, ports and airspace to Qatari-linked travel and traffic.

Qatar has multiple major projects underway (notably, the 2022 FIFA World Cup), which are reliant on imported materials, staff and labour. The Qatar Restrictions therefore significantly impact the construction industry, and potentially required overnight changes in procurement, supply and logistics.

Managing these changes inevitably takes time and involves additional costs and it is often assumed that events like the Qatar Restrictions automatically entitle contractors to relief under contractual 'force majeure' provisions. However, while relief is potentially available under the FIDIC Contracts, actually obtaining it requires careful consideration.

"Force majeure"

As a starting point, a force majeure event must have occurred. A distinction must then be made between the legal doctrine of *"force majeure"* found in civil law jurisdictions, which entitles parties to certain relief (e.g. Article 273 of the UAE Civil Code with similar provisions in the Qatari Civil Code and other codes around the GCC), and contractual *"force majeure"* provisions by which parties allocate the risk of particular events.

The FIDIC Contracts contain a contractual *"force majeure"* provisions in Clause 19. "Force Majeure", defined as an event or circumstance which:

- is beyond a party's control;
- could not have reasonably been provided against;
- cannot reasonably be avoided or overcome;
- is not substantially attributable to the other party; and
- is exceptional.

Clause 19 then provides a non-exhaustive list of the kinds of events or circumstances which may constitute Force Majeure (provided the above criteria are satisfied) and includes, amongst others, war, hostilities and acts of foreign enemies.

At first glance, the Qatar Restrictions seem to fulfil most, if not all, of the criteria for Force Majeure. However, each case must be examined on its own facts.

One difficulty for contractors – and a challenge we have seen raised in respect of the Qatar Restrictions – will be whether the event or circumstances could reasonably be avoided or overcome.

For day-to-day, easily-obtainable items, the event may be easily avoided or overcome, with delays and costs limited and mitigated. For other items, such as long-lead or specialist items, the situation may be different. These may have already been purchased or ordered (often at considerable cost), locked into problematic shipping routes or held at closed borders and ports. The efforts necessary to overcome or avoid these latter events (if possible) may be particularly onerous or costly and it may be unreasonable for contractors to bear responsibility for these alone.

What is "reasonable" will depend on the facts of each case, but is likely to be a contentious issue. Contractors should consider carefully what can reasonably be done to overcome or avoid the event – and do it – as early as possible.

Prevention

Simply establishing Force Majeure will not entitle a contractor to relief. Nor, generally, will it be enough to show that performance is simply more costly and / or will take longer. To be entitled to relief, the FIDIC Contracts require a contractor to show that it is, or will be, "prevented" from performing any of its obligations by the event.

What is the extent of that prevention? Is it enough to demonstrate that the contractor will be prevented from performing within the time for completion required by the contract? Or must the contractor demonstrate that it will be prevented from performing at all?

The FIDIC Contracts provide no definition or explanation of "prevention", leaving this open to argument and interpretation. Usually, this is done in the context of the contract's governing law.

In civil code jurisdictions, only absolute 'impossibility' will usually qualify for relief due to force majeure under the governing law (as opposed to contractually) – it must be impossible to perform the relevant obligations as originally contemplated or through alternative means (though that impossibility may be partial or temporary).

Under the FIDIC Contracts, the contractor's entitlement to time and money due to Force Majeure would suggest that absolute impossibility may not be required. More difficult questions arise where a contract makes performance in a particular manner an essential condition – for example, delivery by a particular route. While the end result may still be achievable (by another route), it cannot be achieved as precisely specified and this may entitle contractors to relief. The nature, scope and terms of the contract will therefore be paramount in determining what is actually "impossible".

Contractors must therefore consider carefully their precise contractual obligations, whether they are in fact prevented or performance is possible by alternative means and whether the contract permits those alternatives.

Notices

An extremely important precondition to obtaining any relief under the FIDIC Contracts is the giving of proper notices. Once the existence of Force Majeure preventing performance is identified, contractors must give employers adequate notice of Force Majeure and specify the obligations affected. Clause 19.2 requires this notice to be given within 14 days after contractors become aware, or should have become aware, of the Force Majeure event.

However, are contractors required to notify within 14 days notwithstanding that it may be unclear if performance will actually be prevented or are contractors only required to provide notice within 14 days after becoming aware that performance definitely has been or will be prevented?

The FIDIC Contracts are not entirely clear. The prudent approach is for contractors to give notice as soon as possible after a Force Majeure event has arisen – even if the effects are not yet clear – and to notify again when they become clearer. This requires contractors to be forward-thinking and proactive in both contract management and predicting the contractual obligations likely to be prevented.

Time and money

Assuming the first three hurdles are overcome – a Force Majeure event, prevention and notices – contractors will be excused from performance of the affected obligations while the Force Majeure prevents their performance .

However, there is no automatic right to additional time or money. Contractors must demonstrate that they have suffered delay or incurred additional "Cost" (as defined under the FIDIC Contracts) as a result of the prevention.

Contractors will only be entitled to additional time if they can demonstrate critical delays and additional "Cost" if the event is of the kind listed in the FIDIC Contracts and, for some of those events, only if they occur in the country of the project.

The wording of the FIDIC Contracts again raises issues for "Cost" claims. For example, what kind of Force Majeure are the Qatar Restrictions and in which country are they occurring?

The Qatar Restrictions do not neatly fit into any of the categories listed in the FIDIC Contracts. Moreover, it could be argued (and we have seen employers do so) that the Force Majeure is not occurring in Qatar (e.g. if the circumstance preventing performance is the closure of a UAE port to Qatari-bound vessels).

These issues can be very contentious. Contractors must therefore think carefully about the relevant event, what kind of force majeure it is and where it is taking place.

"Subject to Clause 20.1"

The FIDIC Contracts treat a Force Majeure claim like other claims: entitlement to additional time or Cost is subject to Clause 20.1. Clause 20.1 requires additional notices, including an initial notice, a detailed claim, interim notices (for continuing effects) and a final claim. These are in addition to notice under Clause 19 and a failure to provide these may frustrate any claim for additional time or money.

These requirements add another procedural hurdle and call for greater vigilance in contract management.

Conclusion

The Force Majeure provisions in the FIDIC Contracts can be a minefield. Force Majeure claims involve many hurdles, and potential pitfalls, and may be highly contentious. However, the potential impacts of events like the Qatar Restrictions means that, notwithstanding these difficulties, claims will inevitably be made to protect contractors' positions.

Establishing an entitlement to relief will require careful preparation, requiring contractors to be on top of potential claims and contractual requirements as early as possible.

Contractors should therefore seek legal advice, as early as possible, to ensure that these hurdles are cleared.

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Australian High Court Limits Grounds for Judicial Review of Adjudication Determinations

The High Court of Australia has ruled that adjudication determinations made under the NSW and SA Security Of Payment Acts are not subject to judicial review for any non-jurisdictional errors of law. The decision, which has wide-ranging consequences, limits the ability to challenge a determination to jurisdictional errors of law only.

In the recent decision of *Probuild Constructions (Aust) Pty Ltd v Shade Systems Pty Ltd & Anor (Probuild)* the High Court of Australia determined that the Supreme Court of New South Wales (NSW) did not have jurisdiction to make an order in the nature of certiorari to quash an adjudicator's determination for a non-jurisdictional error of law, notwithstanding no specific wording to that effect in the Building and Construction Industry Security of Payment Act 1999 (NSW) (SOP Act) *(Probuild Constructions (Aust) Pty Ltd v Shade Systems Pty Ltd & Anor [2018] HCA 4)*. (An order of certiorari quashes a decision of an administrative body.)

Probuild and Shade Systems Pty Ltd (Shade) were parties to a subcontract. Shade served Probuild with a payment claim under the SOP Act, Probuild issued a payment schedule and disputed the entirety of the claimed amount and argued that it was entitled to set off a considerably higher amount for liquidated damages.

In response to the payment schedule Shade referred the matter to adjudication. The adjudicator rejected Probuild's set-off argument, on the basis that liquidated damages could not be calculated until either "practical completion" or termination of the subcontract had occurred.

Probuild applied for judicial review of the adjudicator's determination, claiming that there was an error of law on the face of the record and sought an order in the nature of certiorari quashing the adjudicator's determination pursuant to s. 69 of the *Supreme Court Act 1970*. The Supreme Court of NSW granted the order, stating that the adjudicator had made an error of law when he found that there was no entitlement to liquidated damages until "practical completion".

The decision of the Supreme Court was then appealed to the Court of Appeal of NSW and the High Court of Australia. The High Court found that the Supreme Court of NSW did not have jurisdiction to quash the adjudication determination.

Specifically, the High Court ruled that the purpose of the SOP Act was to put in place an expeditious, inexpensive and informal procedure for the purposes of settling payment disputes between respective parties. The High Court held that these fundamental characteristics of the SOP Act would be thwarted if judicial review was available for every error of law, and that the right to an appeal for an error of law would also delay prompt enforcement of the determinations, and therefore the prompt transfer of progress payments.

The High Court found that it was an inherent part of the SOP Act that adjudication determinations would not be subject to costly and timely appeals on non-jurisdictional errors of law.

Notably, the case was jointly heard with *Maxcon Constructions Pty Ltd v Vadasz* [2018] HCA 5, the consequence of which was that the position has now also been confirmed in relation to appeals under the South Australian Security of Payment legislation[1].

There are numerous consequences for parties seeking adjudication under the SOP Act. The first is that those parties seeking to challenge a determination will first need to show that a jurisdictional error of law was made by the adjudicator. This will require the party to undergo a complex legal exercise of scrutinizing the adjudicator's compliance with the SOP Act's procedures to ensure that the adjudicator has acted within their jurisdictional authority.

Secondly, it highlights the importance of making strong and comprehensive legal submissions on all disputed issues during the adjudication process, because if the adjudicator makes a mere non-jurisdictional error of law, this will not be grounds to have the determination quashed.

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1. Building and Construction Industry Security of Payment Act 2009 (SA).

Conferences and events

Offshore Pipeline Technology Conference
Design Liability
Amsterdam
27 February 2018
Presenting: Michael Sergeant

Training Seminar on the new FIDIC Contracts 2017
Second Editions of the Red, Yellow and Silver Books
Istanbul & Ankara
27-28 February 2018
Presenting: Ben Mellors (in association with ICM Consulting)

Construction Quarterly Seminar
Interpretation of contracts and design liability
London, HFW Office
27- 28 February 2018
Presenting: Max Wieliczko, Katherine Doran

HFW - Diales Seminar
Extensions of time
Melbourne
28 February 2018
Presenting: Nick Longley, Alex McKellar

HFW - Diales Seminar
Extensions of time
Perth
7 March 2018
Presenting: Matthew Blycha, David Ulbrick

HFW – Driver Trett Seminar
KSA Dispute Resolution, PPP and Cost Claims
Riyadh
20 March 2018
Presenting: Beau McLaren

HFW - Diales Seminar
Prolongation cost
Melbourne
28 March 2018
Presenting: Nick Longley, Alex McKellar

Hardwicke Chambers Conference
Middle East Dispute Resolution
Dubai
17 April 2018
Presenting: Beau McLaren

HFW - Diales Seminar
Prolongation cost
Sydney
18 April 2018
Presenting: Ian Gordon, Nick Watts

Construction Quarterly Seminar
London, HFW Office
15 - 16 May 2018
Presenting: Max Wieliczko, Ben Mellors, Richard Booth, Katherine Doran

HFW - Diales Seminar
Prolongation cost
Perth
May
Presenting: Matthew Blycha, David Ulbrick

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