Annual Review of English Construction Law Developments

An international perspective

July 2020

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I simply consider this to be 'mandatory literature' for anyone interested in construction law.

General Counsel, Global Energy Company

Introduction

Welcome to the 2020 edition of our internationally focused *Annual Review of English Construction Law Developments*.

Prompted by recent caselaw on the topic, last year's *Annual Review* contained a detailed overview of the causation requirements for claims under force majeure clauses, with particular reference to the FIDIC forms. Force majeure is now a topic of intense interest in the wake of the coronavirus pandemic. There have been further developments within English law and we revisit the topic in this year's edition with a focus on claims arising from the pandemic.

Another theme continued from last year's *Annual Review* is the impact of the Supreme Court's decision in the *Rock Advertising* case. As anticipated, the application of the decision by the English courts is leading to an increase in informal contracts or arrangements which are found to be of no legal effect. The scope of the decision has also widened this year, with the same principles being applied to "no waiver" clauses and variations made pursuant to contractual formalities being subject to entire agreement clauses in the original contract.

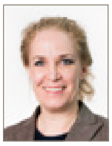
This year's *Annual Review* contains updates on decisions elsewhere in the common law world of relevance to the international construction industry. A decision of Australia's highest court has overturned a longstanding English law doctrine which permits a contractor to ignore the contract sum and claim for the reasonable price of its work in the event of termination. This decision may lead to similar arguments being made in other common law jurisdictions.

Another Australian decision provides a helpful insight into the difficulties which can arise where delay experts are unable to agree on appropriate delay analysis methodologies. A Hong Kong decision appears to be the first to consider provisions roughly equivalent to the new FIDIC Second Edition claims notification provisions, with some notable consequences. And a recent ICSID decision has developed the emerging jurisprudence for investment treaty claims in respect of international construction contracts.

Also included in this year's *Annual Review* is an overview of the new FIDIC Emerald Book as well as coverage of English court decisions on the meaning of "completion", paying sub-contractor's directly and whether liquidated damages for delay continue to accrue after termination.

As always, we hope you find this publication of use and welcome any comments or feedback you may have. Should you wish to receive more frequent updates throughout the coming year, please feel free to sign up for our Law-Now service at **www.law-now.com** and select "Construction" as your chosen area of law.

Finally, we sincerely hope that you and your staff have not been affected by the events of this year in any serious or long-lasting way. We remain on hand for any assistance you may require throughout this period.



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Force majeure: considering the impact of Covid-19

Force majeure clauses have come under particular scrutiny in light of the coronavirus pandemic. For construction projects, the pandemic has birthed various forms of disruption, from the scarcity of materials to total site shutdowns imposed by government authorities, employers or superior contractors. The extent to which a party may claim in respect of such disruption under the terms of their construction contract, as well as the options available for exiting the contract, have become issues of universal significance across the global construction industry. In last year's Annual Review we provided a comprehensive overview of the issues of causation which arise under most force majeure clauses including those under the FIDIC forms. We revisit this topic in the article below, considering English law developments over the past year and the treatment of pandemic claims under the FIDIC form.

Introduction

Force majeure clauses are commonly found in international construction contracts. They typically excuse a party from performance and/or allow a right of termination upon the happening of events which render performance of the contract impossible, whether temporarily or permanently. A force majeure clause may apply only to certain events or generally to matters beyond the control of the parties.

Such clauses typically require a force majeure event to have "prevented" performance of the contract. The FIDIC 1st Editions (all versions) permits the giving of a Force Majeure Notice where a party is "*prevented from performing any … obligations under the Contract*". Performance of such obligations is then excused "*for so long as such [Force Majeure Event] prevents [the party] from performing them*". The FIDIC 2nd Edition is in the same terms, save that Force Majeure Events are now referred to as Exceptional Events.

Such language gives rise to a number of questions as to when work can be said to be sufficiently "prevented" for the purpose of a force majeure claim. As discussed in more detail in last year's *Annual Review*:

- The usual interpretation of the word "prevent" in a force majeure clause requires physical or legal impossibility to be present: "*economic unprofitableness is not 'prevention'" (Comptoir Commercial Anversois v Power, Son & Co).*
- Under English law there is a well established distinction between force majeure clauses which refer to the "prevention" of performance and those which refer to "delays" in performance: *Fairclough Dodd & Jones v Vantol (JH).*
- In construction contacts, the distinction is an important one because a force majeure event is more likely to "delay" completion beyond the contractual completion date, than it is to make completion by that date impossible when all accelerative measures are taken into account (i.e. to "prevent" completion by that date).
- Certain contracts, such as the LOGIC form, include within their force majeure clauses rights of recourse for both prevention and delay. As noted above, however, the standard FIDIC wording refers only to prevention. Claimants under the FIDIC form are therefore required under English law to identify the particular contractual obligation the performance of which is said to have become impossible by virtue of the Force Majeure / Exceptional Event. If the obligation to complete by the Time for Completion is advanced, the contractor will need to show that the delays relied on were impossible to avoid even with accelerative measures.
- Other obligations which might potentially allow a contractor to advance a more traditional delay claim are the obligation to proceed with "*due expedition and without delay*" under Clause 8.1 and the obligation to "*proceed in accordance with the Programme*" in Clause 8.3. However, whether a Force Majeure / Exceptional Event which has delayed completion can be said to have prevented the performance of those obligations is unclear.
- Other difficulties arise where there is more than one cause of delay. Where two causes combine to impact the works, and neither on its own would have done so, both will need to be covered by the force majeure clause: *Seadrill Ghana Operations Ltd v Tullow Ghana Ltd*.
- More commonly, where two independent causes would have impacted the works and only one is a force majeure event, recovery will be denied if the force majeure clause is interpreted as requiring a "but for" test of causation: *Classic Maritime Inc v Limbungan Makmur SDN BHD*.

The final point regarding the "but for" test has received further attention in the last year with an appeal judgment in the *Classic Maritime* case. We consider this further below, before turning more specifically to pandemic claims.

The sole cause requirement: *Classic Maritime* on appeal

To recap, Classic, a ship owner, entered into a long term contract of affreightment with Limbungan for the carriage of iron ore pellets from Brazil to Malaysia. Limbungan intended make shipments under the contract using iron ore pellets obtained from an iron ore mine in Brazil. On 5 November 2015 a tailings dam forming part of the mine burst, leading to the cessation of production.

Classic sued Limbungan for failing to make shipments under the contract. As the freight rates were agreed prior to the collapse in demand for steel in 2009, they were more than seven times the market rate at the time the dam burst, giving a sizeable claim for damages.

Limbungan defended the claim on the basis of a force majeure clause in the contract providing that: "*… the Charterers … shall [not] be Responsible for loss of or damage to, or failure to supply, load, discharge or deliver the cargo resulting from: … accidents at the mine or Production facility… always provided that such events directly affect the performance of either party under this Charter Party…*"

Both parties accepted that an "accident at the mine" had occurred. However, Classic argued that due to the collapse in demand for steel, Limbungan would not have been in a position to meet the required shipments under the contract even if the dam hadn't burst. On the facts, the court agreed with Classic and found that Limbungan would not have made the shipments regardless of the production stoppage. This raised an issue as to whether the force majeure clause applied in such circumstances.

Limbungan relied on a previous line of English cases (including a decision of the House of Lords) deciding that force majeure clauses which reflect the common law doctrine of frustration and provide for the immediate termination of a contract (referred to as "contractual frustration clauses") do not require the "but for" test for causation to be satisfied. This mirrors how the doctrine of frustration operates at common law.

Although acknowledging the similarity between the clauses considered by these cases and the clause relied on by Limbungan, the court at first instance emphasised that the clause fell to be considered on its own terms and that the cases relied upon were in any event limited to contractual frustration clauses which brought about the immediate termination of a contract. The clause under consideration was not a contractual frustration clause and the application of the "but for" test was indicated by the references to a failure to supply "*resulting from*" events which "*directly affect the performance of either party*".

Somewhat paradoxically, however, the court only awarded Classic nominal damages on the basis that if Limbungan had been ready, willing and able to make the shipments, it would have been excused from liability under the force majeure clause. Classic's damages claim was calculated by reference to the position it would have been in had Limbungan made the required shipments under the contract (i.e. absent the breach of contract). Although that is an entirely conventional approach to damages, the court found it to be "*unrealistic*" because it ignored why Lumbungan was in breach of contract. Lumbungan was in breach not simply because it didn't make the shipments, but because the force majeure clause did not excuse non-performance due to Lumbungan not being ready and willing to make the shipments even in the absence of the production stoppage. The correct comparison, according to the court, was with the position that would have occurred had Lumbungan been ready and willing to make the shipments. In that case, the shipments would have been prevented by the production stoppage and the force majeure clause would have applied. Classic had not therefore suffered any loss as a result of Lumbungan's breach and was not entitled to substantial damages.

Appeals were brought by both parties as to the causation and quantum aspects of the respectively. As regards causation, the Court of Appeal agreed with the lower court and eschewed the use of categorisation as an aid to interpretation:

> "*in deciding whether the charterer can rely on clause 32 in circumstances where it would not have performed its obligation anyway, what matters is not whether the clause is labelled a contractual frustration clause, a force majeure clause or an exceptions clause, but the language of the clause. As with most things, what matters is not the label but the content of the tin.*"

The Court of Appeal also found it difficult to say that either party's interpretation was more or less commercial than the other's. Accordingly, the Court approached the interpretation of the clause "*without any predisposition as to the construction which should be adopted and without any need to avoid what are said to be the unfair consequences of adopting one or other of the rival constructions. It is simply a matter of construing the words of the clause.*"

In considering the language of the clause, the Court agreed that use of the phrases "*resulting from*" and "*directly affect the performance of either party*" were supportive of the "but for" test. The Court identified four other aspects of the clause which also supported this conclusion:

— The reference to a "failure to supply" was to be read consistently with other failures covered by the clause i.e. failures to "load, discharge or deliver the cargo". These other failures can only have referred to cargo which, but for the event in question, would actually have been loaded, discharged or delivered.

— The clause contained a large list of force majeure events and it was apparent that some of them were only consistent with the application of the "but for" test such as "seizure under legal process" and "accidents of navigation".

— The events were referred to within the clause as "causes" which supported the impression given from the phrases "resulting from" and "directly affect the performance of either party" that the "but for" test was to apply.

— The clause also provided (after the passage quoted above) that if "any time is lost due to such events or causes", it would not count as Laytime or demurrage. Previous cases had held that time would not be "lost" in such circumstances unless the party in question would have performed in the absence of such an event. This supported the application of the "but for" test to the clause as a whole, as it would be illogical for this part of the clause to provide for a different causation criterion to the rest of the clause.

In relation to quantum, the Court overturned the lower court's decision, finding that a simple comparison with the position Classic would have been in had the shipments been made was the correct approach. Looking beyond the breach itself into the reasons for the failed shipments was impermissible:

> *"Although the judge described his approach as an application of the compensatory principle which was realistic because it took account of the reason why the charterer was in breach of its duty to supply the cargoes, this was in my judgment an irrelevant consideration in the assessment of damages. There is no case, or at any rate none which was cited to us, in which the reason why a party is in breach of contract has been held to justify, let alone require, a different approach to the compensatory principle."*

In summary, the Court of Appeal's decision provides support for the application of the "but for" test to force majeure clauses which use causative language. The decision provides a number of drafting observations which are likely to carry over to other clauses. The phrases "*resulting from*" and "*directly affecting performance*" are commonly used in force majeure clauses and are likely to point toward the application of the "but for" test. So will references to "causes" or "time lost" and the enumeration of events or circumstances which are only consistent with the application of the "but for" test. Parties intending a broader application of such clauses will need to pay careful attention their drafting.

Whilst the Court of Appeal's emphasis on the wording of individual clauses is clear, a question remains as to the correct approach to hybrid clauses which allow a party to terminate a contract due to a force majeure event (whether immediately or after a period of time) in addition to being relieved of liability or the obligation to perform. The relevance of the line of cases dealing with contractual frustration clauses may be argued to be greater in such cases.

The Court of Appeal's reversal of the lower court's findings as to quantum also means that arguments over the applicability of a "but for" are likely to carry significant financial consequences. In the result, Classic was awarded damages of just under USD 20m in circumstances where Limbungan would have otherwise been excused from performance due to the dam failure had it been ready, willing and able to perform.

Pandemic claims under the FIDIC form

The starting point for the consideration of pandemic claims under the FIDIC form is the Force Majeure / Exceptional Event clause: clauses 18 and 19 of the Second and First Editions respectively. In broad outline, these clauses provide as follows:

- The terms "Force Majeure" and "Exceptional Event" are defined in general terms as an event or circumstance which:
  - is beyond a Party's control;
  - the Party could not reasonably have been provided against before entering into the Contract;
  - having arisen, such Party could not reasonably have avoided or overcome; and
  - is not substantially attributable to the other Party.
- As noted above, to qualify for relief under the clause, a Force Majure / Exceptional Event must "prevent" a Party from performance any of its obligations under the Contract.
- The affected Party must give notice within 14 days of becoming aware of the event. The Second Edition makes clear that if notice is not given within this period, any entitlement to relief is lost for the period up until notice is given. Upon giving notice, the affected Party is excused from performance of the prevented obligations .
- The affected Party is required to notify the other Party when it ceases to be affected by the event and under the Second Edition, interim notices are required every 28 days to update the other Party on the effect of the event.
- Both Parties are under an obligation to use "all reasonable endeavours" to minimise any delay arising as a result of the event.
- If the Contractor is the affected Party, and suffers delay as a result of the event, it is entitled to an extension of time. It is also entitled to recover any additional Cost incurred as a result of the event if the event is one specifically listed in clause 18.1 or 19.1 of the Second and First Editions respectively.
- If execution of substantially all the Works in progress is prevented for 84 continuous days, or 140 cumulative days due to the same event, then either party may terminate the Contract. Additionally, if any event arises outside the control of the Parties (whether or not a Force Majeure / Exceptional Event) which makes performance impossible or unlawful, or which under the applicable law entitles the Parties to be released from further performance of the Contract, either Party may terminate immediately unless (under the Second Edition) the they are able to agree on an amendment to the contract that would permit continued performance.

Under English law, and unlike most civil law countries, there is no distinct legal doctrine of force majeure. Questions of force majeure only arise under English law where the term is used in a contract and calls for interpretation. In such circumstances, English judges have been willing to draw from civil law jurisprudence, in addition to applying the usual English approach to interpretation. For example in *Lebeaupin v Richard Crispin & Co* the following statement of the meaning of "force majeure" in French law by Goirand was said to be applicable to many English contracts:

> *"Force majeure. This term is used with reference to all circumstances independent of the will of man, and which it is not in his power to control … thus, war, inundations and epidemics are cases of force majeure; it has even been decided that a strike of workmen constitutes a case of force majeure."*

The mention of epidemics suggests that the Covid-19 pandemic would fall within the phrase "force majeure" when used in English contracts. The general definition of Force Majeure / Exceptional Event under the FIDIC form outlined above is also likely to cover the pandemic. The more difficult issue of categorisation lies in whether the pandemic can be classified as one of the specific events listed in clause 18.1 / 19.1. This is required in order for the Contractor to be entitled to recover additional Cost as a result of the pandemic.

Three specific events might be said to have relevance:

- "*lockout*" by persons not connected with the Contractor or its subcontractors; a government imposed shutdown of construction sites may qualify under this heading;
- "*disorder*" by persons not connected with the Contractor or its subcontractors; government imposed lockdowns and the furloughing of large workforces might be argued to amount to disorder, given the similarities with "strikes", another listed event;
- "*natural catastrophes*" such as earthquake, tsunami, hurricane, typhoon or volcanic activity; although distinct from the climatic and geological forces exemplified in this list, it might be said that the micro-biological force of a pandemic may also amount to a natural catastrophe.

Aside from classification of the pandemic, causation is likely to feature strongly in the debate over pandemic claims. In many countries, including England, Government authorities have not banned the carrying out of construction work, but have issued guidance as to the additional distancing and safety measures to be adopted to prevent the spread of the virus. Such measures will in many cases have significantly reduced the progress able to be achieved, particularly during the initial phases of the pandemic where distancing and lockdown measures were at their height. Contractor's will wish to present claims for the delay caused by such reductions in productivity by simple comparisons with the progress which would otherwise have been made in the absence of the pandemic. However, this brings into focus FIDIC's use of the word "prevent" as the pre-condition to entitlement in Force Majeure / Exceptional Event claims. Employer's may argue that accelerative measures at the Contractor's expense are now possible after the easing of pandemic conditions and that the pandemic has not "prevented" timely completion in the sense of making it impossible, even though such accelerative measures may come at considerable expense. Arguments exist for Contractor's to resist such a position, as identified above and in more detail in last year's *Annual Review*, but the position is far from clear under the standard FIDIC wording.

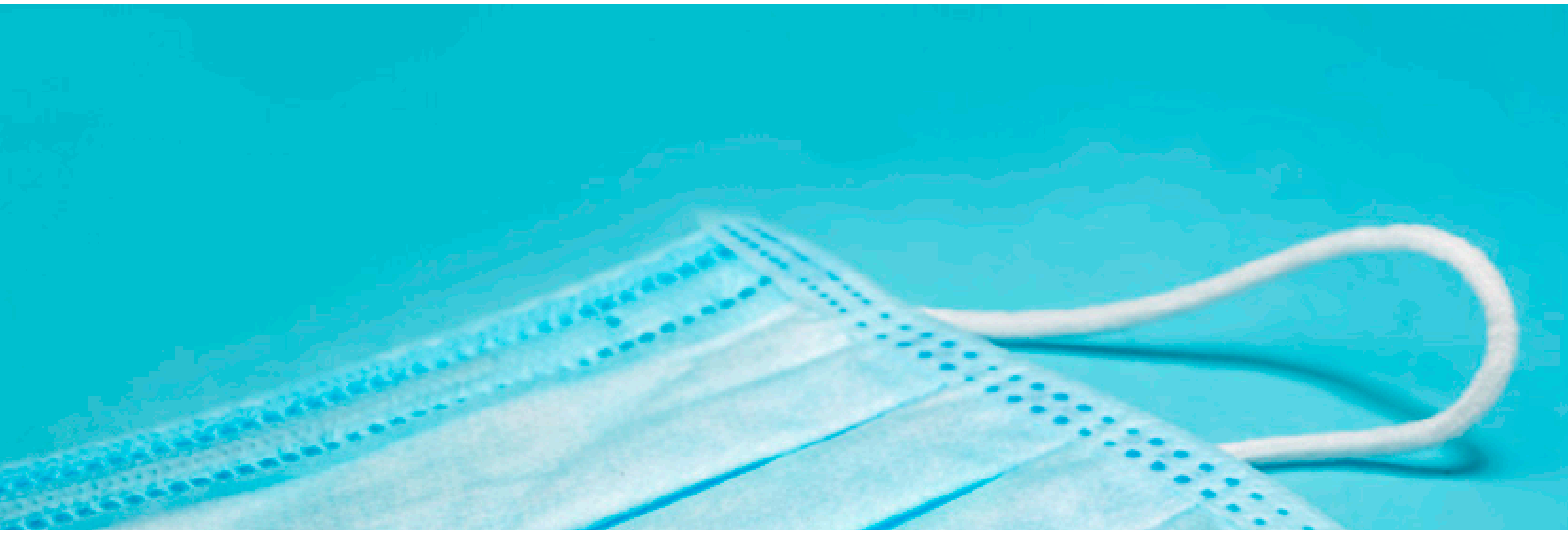
A separate source of dispute is likely to arise in relation to other potential causes of disruption alongside the pandemic. The extent to which a Contractor may have already been facing delays when pandemic measures came into effect is likely to be something which many Employer's are keen to explore. The Court of Appeal's decision in the *Classic Maritime* case is likely increase debate over whether a "but for" test of causation applies to the FIDIC Force Majeure / Exceptional Event provisions. There are reasons to think that such a test would apply. The FIDIC provisions require prevention of performance "*by Force Majeure*" (Clause 19.2, First Editions) and "*due to an Exceptional Event*" (Clause 18.2, Second Editions). These are causative phrases. The concept of "prevention" itself has also been found under English law (albeit not without controversy) to imply a "but for" test, such that where a delay would have occurred anyway in the absence of the event claimed for, no "prevention" will in fact have occurred: *Jerram Falkus Construction Ltd v Fenice Investments Inc.*

Against these arguments, could be put the right of termination included within the FIDIC provisions, which might be said to bring those provisions closer to the "frustration clauses" which have been held not to import a "but for" test for causation. However, these rights are also expressed in terms of progress in the works being "*prevented*" for the relevant period of time "*by reason of*" a Force Majeure / Exceptional Event. The drafting of the more general right to terminate in circumstances of impossibility, illegality or release from further performance under the applicable law is also relevant. There, the event is required to "*make it impossible or unlawful for either or both Parties to full its or their contractual obligations*". Such language is more consonant with a frustration clause which does not require a "but for" criterion to be satisfied.

Conclusion

As noted in last year's Annual Review, significant points of uncertainty exist as to the operation of force majeure clauses in a construction context under English law. Many of these uncertainties will be brought into sharp focus by the disruption facing the global construction industry as a result of the coronavirus pandemic. The many pandemic claims which will need to be resolved may provide greater certainty over the long term. In the meantime, parties should take care to analyse pandemic claims closely and be aware of the difficulties which may beset them.

References: *Lebeaupin v Richard Crispin & Co* [1920] 2 K.B. 714; *Comptoir Commercial Anversois v Power, Son & Co.* [1920] 1 KB 868; *Fairclough Dodd & Jones v Vantol* (JH) [1957] 1 WLR 136; *Jerram Falkus Construction Ltd v Fenice Investments Inc* [2011] EWHC 1935 (TCC); *Seadrill Ghana Operations Ltd v Tullow Ghana Ltd* [2018] EWHC 1640 (Comm); *Classic Maritime Inc v Limbungan Makmur SDN BHD* [2018] EWHC 2389 (Comm); *Classic Maritime Inc v Limbungan Makmur SDN BHD* [2019] EWCA Civ 1102.



Liquidated damages and termination

A English Court of Appeal decision has provided guidance as to the effect of termination on liquidated damages provisions in relation to delay. The decision resolves conflicting authorities on this issue stretching back more than a century, but has since been appealed to the Supreme Court (the UK's highest court) and is due to be heard there later this year. The Court of Appeal's reasoning has significant implications for parties considering termination scenarios as it suggests that many liquidated damages provisions providing compensation for delay may fall away entirely on termination of the contract, leaving the employer to prove a claim for general damages for delays both before and after termination.

Termination and liquidated damages clauses

Whether a clause entitling an employer to claim liquidated damages for delay will survive termination has been decided inconsistently in previous cases. A decision of the House of Lords (the UK's highest court, now called the Supreme Court) in 1912 decided that such a clause applied only where the original contractor completed the works and was not applicable upon termination *(British Glanzstoff Manufacturing v General Accident, Fire and Life Assurance Co*). However, this decision appears to have been overlooked in the modern cases.

More recent cases have held that liquidated damages accrue up until the date of termination, but not thereafter. The employer is then left to bring a general claim for unliquidated damages for post-termination delays. Other recent cases have held that liquidated damages continue post-termination until the works are completed by the employer or a new contractor. The justification for this is said to be that any other approach would reward the contractor for its own default. This was the line taken most recently by the *English Commercial Court in GPP Big Field v Solar EPC Solutions*.

The Court of Appeal

The Court of Appeal upheld Triple Point's appeal on this point and found that no liquidated damages accrued for incomplete milestones in circumstances of termination. Lord Justice Jackson set out the three inconsistent lines of authority identified above, noting that *British Glanzstoff* had not been cited in the modern cases despite it being "*a decision of our highest court, which has never been disapproved*".

Although the outcome in each case depends on the precise wording of the clause in question, the Court of Appeal expressed doubts about the cases which permit liquidated damages for delay to persist beyond termination. This echoes criticism made by commentators in relation to these cases.

The Court also identified difficulties with the view, favoured by most textbooks, that liquidated damages apply up to the date of termination, but not beyond. Whilst this might be said to preserve accrued rights, it may be artificial to divide the employer's right to damages for delay into a period of liquidated damages prior to termination and a period of general damages after termination: "*It may be more logical and more consonant with the parties' bargain to assess the employer's total losses flowing from the abandonment or termination, applying the ordinary rules for assessing damages for breach of contract.*"

The clause before the Court specifically referred to liquidated damages accruing "*up to the date PTT accepts such work*". This was similar to the wording considered in *British Glanzstoff* in that the completion of the work was expressly contemplated. Accordingly, the proper interpretation was that the entitlement to liquidated damages in respect of incomplete milestones fell away entirely upon termination and was replaced by a right to claim general damages for delay, subject to proof by PTT.

The Supreme Court and beyond

As noted in the introduction, the Court of Appeal's decision is presently on appeal to the Supreme Court. Whilst each case will depend on the drafting of the clause in question, the reasoning favoured by the Court of Appeal would mean that clauses which refer expressly to liquidated damages accruing until the completion of the works are more likely to fall away entirely upon termination in accordance with the *British Glanzstoff* decision. A large number of construction contracts are drafted in this way, including the FIDIC forms.

Employers considering the termination of a construction contract where the contractual date for completion has been overrun should carefully consider the implications of this decision. Termination in such circumstances may mean that any entitlement to liquidated damages for delay no longer applies, requiring the employer to prove actual delay losses. These may be more or less than the level set for liquidated damages – or difficulties of proof may in some circumstances render them irrecoverable. Arguments may also arise as to whether the liquidated damages provision, albeit inapplicable, remains relevant to the assessment of any claim for general damages. The Supreme Court's decision is eagerly awaited.

References: *British Glanzstoff Manufacturing v General Accident, Fire and Life Assurance Co* 1913 SC (HL) 1; *Triple Point Technology, Inc v PTT Public Company Ltd* [2019] EWCA Civ 230; *GPP Big Field LLP v Solar EPC Solutions SL* [2018] EWHC 2866 (Comm).

The FIDIC Emerald Book

In May 2019 FIDIC launched its new "Emerald Book" – Conditions of Contract for Underground Works. This addition to the FIDIC suite seeks to fill a gap amongst standard forms as a specialist contract for use on underground projects, including tunnelling works. We provide an overview of the key features of the Emerald Book below.

A new approach to risk allocation

The Emerald book sets out a distinctive approach to risk allocation designed specifically with underground projects in mind. In particular:

- Risk allocation is based on a Geotechnical Baseline Report ("GBR") and a Schedule of Baselines and Geotechnical Data Report ("GDR").
- The intention is that Employer should carry out significant investigations prior to tendering the works to obtain as much information as possible regarding subsurface risk (including water risks).
- Foreseeable risks (i.e. those risks identified in the GBR) are allocated to the party best placed to manage them.
- The Employer takes the risk associated with conditions worse than those set out in the GBR, but also gets the benefit where conditions are more favourable than those set out in the GBR – the Time for Completion time can be shortened and the Contract Price reduced.
- The Contractor assumes the risk of delivering the works where conditions are as per those expected in the GBR – the Contractor designs the works in accordance with the GBR and the Employer's Requirements.
- Any subsurface conditions outside the scope of the GBR are deemed to be Unforeseeable, entitling the Contractor to additional time/money. Other physical conditions are claimable if Unforeseeable in the usual way (i.e. not reasonably foreseeable by an experienced contractor at the Base Date).
- The Contractor is required to complete and maintain a Contract Risk Register and prepare and maintain a Contract Risk Management Plan (concepts familiar from the NEC suite of Contracts) – recognition that much can go wrong in projects of this nature.

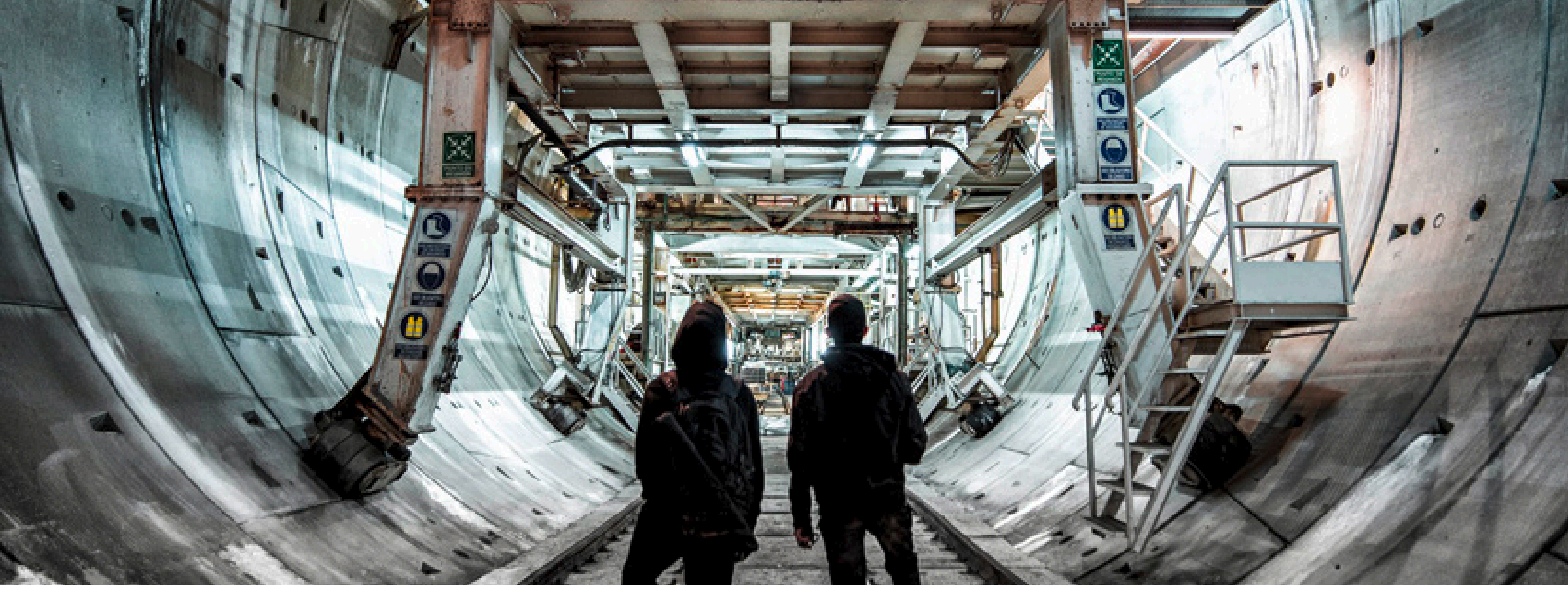
Excavation and lining works

Specific provision is made for excavation and lining works:

- These works are recognised as being a key part of the Works themselves, and difficult to accurately scope out/quantify at tender stage.
- These works are therefore paid for on a remeasurement basis - rates and prices are set out in the Bills of Quantities.
- These are divided into Fixed rate items, Time related rate items and Quantity related rate items.
- These rates also allow a mechanism for valuation of prolongation costs in the event of Unforeseeable subsurface conditions being encountered.

Payment and performance security

- Provision is made for an Advance Payment Guarantee as well as Performance Security to be delivered by the Contractor. Advance payments are likely to be necessary where high value plant is to be paid for up front.
- There is provision for a JV Undertaking – to provide for joint and several liability between the JV parties, to allocate a leader and to set out their individual scopes where relevant.
- As in other FIDIC contracts, the Employer must provide details of its financial arrangements for the project, and revisit these where project costs increase.



Engineer's role, dispute avoidance and resolution

The roles of the Engineer and the dispute resolution provisions of the Emerald Book are similar to those in other FIDIC books:

- The Engineer acts as Employer's Agent and has specific role in respect of monitoring progress of the excavation and lining works
- The Engineer is also required to determine certain matters as between the parties. There is a specific statement that the Engineer will act impartially in this role. The Engineer must be wary of conflicts of interest.
- Where either party is dissatisfied with the Engineer's decision the matter is referred to a Dispute Avoidance/Adjudication Board (appointed for the duration of the contract).
- Where either party remains dissatisfied, the matter will be referred to arbitration under the ICC rules.

Considerations for early adopters

Those parties considering adopting the new Emerald Book may wish to give thought to the following additional considerations:

- The agreement of the GBR is likely to be an involved process requiring significant negotiation. As this is so central to the contract (with time and cost both hinging on it) it will be crucial to get it right before it becomes contractual.
- As with other FIDIC forms, the Emerald Book places a fitness for purpose obligation on the Contractor. The Employer will need to ensure that the intended purpose is stated clearly in the Employer's Requirements in order to benefit from this – including any expected lifetime of the works.
- The Contract provides that the Employer is required to obtain all permits, licenses and consents stated in the Employer's Requirements to be its responsibility, and that the Contractor is required to obtain any others. The Employer is also responsible for allowing the Contractor access to the Site – which could be complicated in respect of tunnelling contracts affecting ground in the ownership of a number of different parties. It will remain important to ensure that the full jigsaw of permissions and consents is in place prior to work commencing, and that sufficient time is allowed for this exercise (as negotiations could be lengthy).
- The Contractor is required to take measures to limit nuisance to third parties but it is likely that in tunnelling projects third party interests will need to represented much more robustly than this. In particular, landowners consenting to tunnelling under their property are likely to require collateral warranties with clear undertakings as to the manner of working, ability to call upon the Contractor's insurances and perhaps even rights to scrutinise and input into methodology, as well as indemnities in event of any loss being suffered. Additional contractual provisions are likely to be driven by discussions with the third parties themselves.
- Although an Advance Payment Guarantee is provided for, the Employer may wish to consider whether further comfort is required in respect of expensive tunnelling equipment or specialist materials. Where costly items are paid for in advance, ownership may be agreed to vest in the Employer as the item(s) is/are fabricated (before shipment/delivery). It is never possible to provide a 100% safeguard against supplier insolvency, particularly where dealing with foreign suppliers, but direct contractual links can assist. Seeking advice in respect of insolvency laws in the local jurisdiction may also be prudent.

“No oral modification” and “no waiver” clauses: the fallout from *Rock Advertising* continues

In last year’s Annual Review we reported on a decision of the Supreme Court (the UK’s highest court) which had reversed previous decisions in finding that “no oral modification” or “anti-variation” clauses were effective to bind parties as to the mode by which subsequent variations must be made. This decision has particular relevance for construction projects where variations and other agreements are often discussed informally among the project teams for each party. A number of cases in the short period after the Supreme Court’s decision have struck down informal agreements due to a failure to observe the formalities prescribed by the contract. In 2019, two further decisions have clarified the reach of the Supreme Court’s decision by extending it to “no waiver” clauses and finding that variation agreements made in accordance with a no oral modification clause may themselves be subject to an entire agreement clause within the original contract, effectively imposing a further requirement on the making of such variations.

Introduction

Large international construction contracts are typically administered for Employers and Contractors alike by project managers or engineers within defined project teams. In a FIDIC context, these positions are occupied by the Engineer and the Contractor’s Representative (and any of their delegates or assistants). Throughout the course of a project, these personnel will discuss a broad range of issues, including technical matters, financial details and the legal merits of particular positions adopted by either party. As they are appointed by the parties and given responsibility for the management of such issues, these personnel will usually have authority to conclude agreements on behalf of the parties or to make statements which have legal effect under the relevant construction contract. Given that project level discussions often take place informally, risks arise that agreements or statements may be made without proper consideration or without prior approval of senior management. So called “no oral modification clauses” (“NOM clauses” for short) and “no-waiver” clauses are often included within construction contracts to protect against these risks.

NOM clauses will typically seek to preclude the making of variations or amendments to a contract unless certain formalities are followed. A popular form is to require that any amendment be “in writing and signed by the parties”. “No-waiver” clauses are similar and will usually seek to preclude informal waivers of rights by stating that any waiver must be in writing and signed by the party concerned. In a construction context, NOM clauses are often drafted to preclude payment for varied or additional work unless agreed or instructed in writing by the Employer or the Employer’s engineer or architect.

The effectiveness of these clauses has long been questioned on the basis that freedom of contract requires that parties be able to make new contracts through whatever means they choose and they cannot therefore put beyond their power their ability to do so in the future. Others argue that by giving effect to them the courts are upholding an exercise of the parties’ freedom of contract. In 2018, this debate was decisively determined in favour of upholding such clauses by the UK Supreme Court in *Rock Advertising Ltd v MWB Business Exchange Centres Ltd.*

Rock Advertising: a recap

Rock Advertising involved a licence agreement for office space for a fixed term of 12 months. The licence contained a NOM clause in the following terms: "*All variations to this Licence must be agreed, set out in writing and signed on behalf of both parties before they take effect.*"

Six months later, the director of the licensee (Rock Advertising) had a telephone conversation with a credit controller from the licensor (MWB) about payment arrears. The court at first instance found that, during this conversation, a variation to the payment schedule was agreed. However, MWB treated the variation as merely a proposal and ultimately rejected the varied schedule. It then proceeded to lock Rock Advertising out of the premises for failure to pay the arrears and terminated the licence.

The Supreme Court upheld MWB's position, finding that the NOM clause was effective against the oral agreement relied on by Rock Advertising. The Court disagreed that the making of such an oral agreement implicitly dispensed with the NOM clause:

> *"What the parties to such a clause have agreed is not that oral variations are forbidden, but that they will be invalid. The mere fact of agreeing to an oral variation is not therefore a contravention of the clause. It is simply the situation to which the clause applies. … The natural inference from the parties' failure to observe the formal requirements of a No Oral Modification clause is not that they intended to dispense with it but that they overlooked it. If, on the other hand, they had it in mind, then they were courting invalidity with their eyes open."*

The Court also considered the potential for injustice to arise where oral agreements in contravention of an anti-variation clause have been acted upon by the parties who then find themselves unable to enforce the agreement. The Court left open whether the doctrine of estoppel might assist a party in such circumstances, although at the same time identifying a number of difficulties lying in the path of such an argument:

> *"In England, the safeguard against injustice lies in the various doctrines of estoppel. This is not the place to explore the circumstances in which a person can be stopped from relying on a contractual provision laying down conditions for the formal validity of a variation. The courts below rightly held that the minimal steps taken by Rock Advertising were not enough to support any estoppel defences. I would merely point out that the scope of estoppel cannot be so broad as to destroy the whole advantage of certainty for which the parties stipulated when they agreed upon terms including the No Oral Modification clause. At the very least, (i) there would have to be some words or conduct unequivocally representing that the variation was valid notwithstanding its informality; and (ii) something more would be required for this purpose than the informal promise itself …"*

Do the same principles apply to "no waiver" clauses?

In last year's Annual Review we noted that the Supreme Court's decision had already been applied to change control procedures under a contract for software services and was very likely to be applied to similar procedures under construction contracts. We also noted that the decision had been argued to apply to "no waiver" clauses but that no decided case had yet determined the point. That point has now been decided by the English Commercial Court in *Sumitomo Mitsui Banking Corporation Europe Ltd v Euler Hermes Europe SA (Nv)*.

Sumitomo concerned a PFI waste treatment project in Derby, England. The construction sub-contractor provided a performance bond and retention bond to the SPV project company, which fulfils a main contractor role under a PFI contract structure ("ProjCo"). ProjCo assigned its rights to the bonds to a security trustee under the terms of a debenture agreement. The performance bond permitted such an assignment subject to the "*assignee confirming to the Bondsman in writing its acceptance of the Employer's repayment obligation pursuant to clause 8*". Clause 8 obliged ProjCo to repay to the Bondsman any amounts found by a court to have been overpaid under the bond.

The security trustee sent a Notice of Assignment to the Bondsman, but did not confirm its acceptance of the repayment obligation in clause 8. The Bondsman signed a duplicate of the notice noting: "*We acknowledge receipt of the notice of assignment of which this is a copy and confirm each of the matters referred to in the notice of assignment.*"

The security trustee subsequently claimed under the performance bond and the Bondsman argued that there had been no valid assignment due to the failure to confirm acceptance of the repayment obligation under clause 8. The security trustee claimed this requirement had been waived by the Bondsman's acceptance of the Notice of Assignment. The Bondsman relied on a "no waiver" clause in the Performance Bond as follows:

> *"12. Non-Waiver*
>
> *12.1 No failure or delay by either party in exercising any right or remedy under this Bond shall operate as a waiver; nor shall any single or partial exercise or waiver of any right or remedy preclude the exercise of any other right or remedy, unless a waiver is given in writing by that party.*
>
> *12.2 No waiver under clause 12.1 shall be a waiver of a past or future default or breach, nor shall it amend, delete or add to the terms, conditions or provisions of this Bond unless (and then only to the extent) expressly stated in that waiver."*

The court agreed with the Bondsman and considered that *Rock Advertising* applied equally to "no waiver" clauses:

> *"As is made clear in Rock Advertising, the parties to a contract may, in that contract, make provisions which limit the effectiveness which their subsequent dealings might otherwise have had in altering their obligations under that contract. While I accept … that a non-waiver clause can itself be waived, it would appear to me to be inconsistent with … Rock Advertising … to find that any conduct which would amount to a waiver of the original right also amounts to a waiver of the non-waiver clause. In my judgment there would have to be something which showed that there was not only a waiver but a waiver of the non-waiver clause. … there would have to be something which indicated that the waiver was effective notwithstanding its noncompliance with the non-waiver clause and something more would be required for this purpose than what might otherwise simply constitute a waiver of the original right itself."*

The assignment was therefore invalid.

What about "entire agreement" clauses?

Another issue posed by the *Rock Advertising* decision is the interrelationship between "entire agreement" clauses and NOM clauses. Entire agreement clauses ordinarily seek to exclude the ability of a party to rely on representations or statements made during tender negotiations and prior to the execution of a contract. The FIDIC suite of contracts do not contain an entire agreement clause, although they are frequently inserted where English law is applicable. The popular English engineering contract, the NEC, includes a simple entire agreement clause as follows: "*This contract is the entire agreement between the parties.*" Such clauses are often expanded to preclude any reliance by the parties on pre-contractual statements or representations.

Where a contract includes both a NOM clause and an entire agreement clause, a question arises as to the extent to which the entire agreement clause applies to an agreement in writing to vary the contract pursuant to the NOM clause. Such an issue was considered by the English Court of Appeal last year in *NHS Commissioning Board v Vasant.* The case concerned contracts between dentists and a public health authority known as NHS England for the provision of general dental services. These contracts were known as "GDS contracts" and contained both entire agreement and NOM clauses in the following terms:

> *"287. … no amendment or variation shall have effect unless it is in writing and signed by or on behalf of the PCT and the Contractor.*
>
> *366. Subject to … any variations made in accordance with Part 22, this Contract constitutes the entire agreement between the parties with respect to its subject matter.*
>
> *367. The Contract supersedes any prior agreements, negotiations, promises, conditions or representations, whether written or oral…"*

The dentists also supplied certain specific services known as "IMOS" under a separate contract. NHS England wrote to the dentists proposing that the specific IMOS services be included within the broader GDS contract and included a single page Variation Agreement Form ("VAF") to be signed by the dentists containing a simple amendment to the GDS contract to include IMOS services. The VAFs were duly signed by NHS England and the dentists.

NHS England subsequently sought to terminate the IMOS services and this was disputed by the dentists on the basis that the GDS contract did not allow such a termination. The prior IMOS contract did allow such a termination and NHS England claimed that the GDS contract had not been validly amended because the VAFs were too vague and provided no details of the IMOS service or any provisions for payment. The dentists contended that the IMOS contract could be referred to to give the necessary certainty, but NHS England claimed that was prevented by the entire agreement and NOM clause.

The Court of Appeal agreed that the entire agreement clause prevented parts of the IMOS contract being used to supplement the written terms of the VAFs:

"[The NOM clause] requires a variation to be (a) in writing and (b) signed by the parties. The VAF itself satisfies both those requirements. But once a variation has been made, I consider that the GDS contract, as varied, is governed by [the entire agreement clause]. For the purposes of that clause it seems to me that the contract terms consist of (and consist only of) what is contained in the GDS contract itself, and what is contained in the VAF. It is true … that many entire agreement clauses are wholly backward-looking; and do not have any impact on how the parties may alter the terms of their bargain once the contract has been made. But in the present case clause 367 performs that function. In my judgment the combination of [the entire agreement and NOM clauses], taken together, evince a clear purpose of ensuring that all the terms of the bargain are to be found in the combination of the original GDS contract and any written variation compliant with clause 287."

Conclusions

These recent cases underscore the great significance that the Supreme Court's decision in *Rock Advertising* has for contracts of all types. In the 2017 edition of this *Annual Review* we noted that the state of the law at that point meant that NOM and no-waver clauses were unlikely to be given effect, due to the willingness of the courts to find implied agreements to dispense with or waive such clauses. Three years on, the position could not be more different.

Entire agreement and no waiver clauses are very common in international construction contracts and parties negotiating them should consider carefully the impact of these recent decisions. The close co-operation necessitated by construction work lends itself to informal agreements and the drifting of on-site practices from the letter of the contract. The strict application of no waiver clauses given by the court in *Sumitomo* shows that legal acts acknowledged by both parties may subsequently prove to be invalid. The combination of NOM clauses with entire agreement clauses (as is common) means not only must variations be recorded in writing, but the parties must be careful to ensure that the written record is comprehensive.

Parties wishing to sensibly navigate this difficult legal terrain are left with essentially two options. The first is to agree more limited clauses or to remove NOM and no waiver clauses altogether. That involves accepting the risks of unauthorised and/or accidental agreements or waivers which these clauses were designed to protect against. The second option is to accept that the proper operation of such contractual protections requires a much closer involvement of legal resource in the day-to-day management of a project (with the additional cost that entails).

References: *Rock Advertising Ltd v MWB Business Exchange Centres Ltd* [2018] UKSC 24; *Sumitomo Mitsui Banking Corporation Europe Ltd v Euler Hermes Europe SA (Nv)* [2019] EWHC 2250 (Comm); *NHS Commissioning Board (Known As NHS England) v Vasant* [2019] EWCA Civ 1245.

The meaning of "completion"

An English Court of Appeal decision in 2019 has provided guidance as to when completion of construction works will be achieved. Some recent court decisions and the first instance decision of the English Technology and Construction Court in this case had favoured an approach which emphasised the intended purpose of the works. This aligns with the approach taken under the FIDIC forms which permit Completion and Taking Over to occur despite the presence of minor outstanding work and defects which will not substantially affect the safe use of the Works for their intended purpose. However, the Court of Appeal has confined the English common law position to defects which are *de minimis* or no more than trifling. This puts the English common law position out of step with the FIDIC forms and should be kept in mind by those considering amendments to FIDIC-based agreements.

Mears Ltd v Costplan Services (South East) Ltd

Mears entered into an agreement for lease with Plymouth (Notte Street) Limited (the "Developer") to take a 21 year lease of two blocks of student accommodation to be constructed in Plymouth. The Developer engaged a contractor to build the blocks under a JCT Design and Build contract, a popular English form of contract, and appointed Costplan as its Employer's Agent.

The building of the blocks was delayed by almost a year and Mears alleged there were a number of defects in the works. Most notably, Mears claimed that around 50 of the student rooms constructed had been built more than 3% smaller than specified in the agreement for lease.

Mears therefore claimed that "practical completion" of the works could not be certified by Costplan under the agreement for lease. Practical completion is a commonly used term in domestic English construction contracts and is the trigger for the commencement of the defects liability period as well as marking the end date for any liquidated damages accruing after the contractual date for completion. As such, the term is analogous to the concepts of "Completion" and "Taking Over" under FIDIC-based contracts.

The reaching of practical completion in this case was significant because:

- if it did not occur by a longstop date, Mears had the right to terminate the agreement for lease; and
- once practical completion occurred, the Developer was to be released from liability to Mears in certain respects as regards the works.

Mears sought declarations from the court that the reduced size of the rooms amounted to a "material and substantial" defect in the works and that practical completion could not therefore be certified by Costplan.

A purpose driven approach

The English Technology and Construction Court found in Mears' favour that the rooms in question had been built more than 3% smaller than specified. However, the court felt unable to determine whether such a breach of the agreement for lease was "material and substantial" without further evidence. In considering whether practical completion could be certified, the court nevertheless proceeded on the assumption that the breach was material and substantial.

The court considered the usual definition of "practical completion" and concluded that the concept was highly fact dependent. It was not possible to conclude that merely because a defect was material or substantial, practical completion would necessarily be prevented. The court emphasised the intent and purpose of the works. Accordingly, "*any (other than "de minimis") breach of a building contract by the contractor, of whatever kind, could potentially stop practical completion depending on the nature and extent of it and the intended purpose of the building*".

The mere fact that a defect was material, or something other than *de minimis*, was not sufficient. The declarations sought by Mears could not therefore be granted in the absence of a detailed evidence considering the impact of the reduction in room sizes.

The Court of Appeal

Mears appealed on a number of issues. In relation to practical completion, the Court of Appeal made a comprehensive review of the authorities and adopted a narrower approach than the TCC. In the Court of Appeal's judgment, the central question was whether a defect was *de minimis* or trifling. If it was, it would not prevent practical completion. If it wasn't, practical completion could not be certified. In this respect, the court described Mears proposed declaration that practical completion could not be achieved whilst there were material and substantial defects as "*relatively uncontroversial*" (although the court still declined the declaration for other reasons).

In reaching this decision, the court cast doubt on previous cases which had indicated a potentially broader approach (and others which were even stricter). The court also provided helpful guidance more generally as follows:

1. Practical completion is itself difficult to define and there are no hard and fast rules.
2. The existence of a latent defect will not prevent practical completion.
3. It makes no difference whether a defect involves an item of work not yet completed or one that has been completed but is defective.
4. The existence of patent defects will be sufficient to prevent practical completion, save where they are *de minimis* or trifling in nature.
5. The ability to use the works as intended may be a factor in considering whether a patent defect is trifling in nature (for example, in this case the fact that the rooms were 3% smaller did not prevent the rooms from being used as student accommodation). However, such an ability does not necessarily mean that the works are practically complete.
6. The mere fact that a defect is irremediable does not mean the works are not practically complete. The question remains whether the defect is trifling in nature.

Conclusions and implications

As noted earlier, the term "practical completion" used in the above cases is analogous to the FIDIC concepts of Completion and Taking Over. Without express qualification, such terms in a FIDIC-based contract would now be likely to be interpreted as signifying the completion of all work without patent defects which are more than trifling in nature. This issue is, however, addressed expressly under both the First and Second Edition FIDIC forms. In the First Editions, Taking Over requires the completion of work "*except for any minor outstanding work and defects which will not substantially affect the use of the Works or Section for their intended purpose*". The Second Editions contain identical phraseology, save that the "safe use" of the Works or Section is referred to, closing a potential argument that the use of the Works or a Section for its intended purpose might be said to be unaffected, despite outstanding safety issues.

Clarity as to the precise requirements for Taking Over is important. Taking Over will usually mark the stepping down of project securities from Performance Bond to Retention Bond, the cessation of any liquidated damages for delay and changes in the insurance of the Works (with risk in the Works passing to the Employer). Whether or not certain defects or incomplete work are significant enough to prevent Taking Over is, for these reasons, often a point of contention. The significance of the standard FIDIC wording in extending the English common law position as to completion should therefore be borne in mind by those considering bespoke amendments. Changes which remove this wording and leave references to "completion" of the works unqualified are likely to result in the English common law position applying, as described above, which is likely to set a much a higher bar for the Contractor.

References: *Mears v Costplan Services (South East) Limited* [2018] EWHC 3363 (TCC); *Mears Ltd v Costplan Services (South East) Ltd [*2019] EWCA Civ 502.

Quantum meruit claims after termination: archaic loophole or viable exit strategy

A decision of the High Court of Australia in 2019 has held that restitutionary claims on a quantum meruit (i.e. reasonable price) basis by contractors after the termination of a construction contract can only be brought in limited circumstances and should be limited by reference to the agreed contract sum. The Court's decision marks a change from the position in most common law jurisdictions around the world (including England) which allow a contractor to claim losses on a quantum meruit basis in excess of the contract price where it has accepted the owner/employer's repudiation of a construction contract. Despite this principle of law existing for more than 100 years, there has been significant criticism of its operation insofar as it undermines the allocation of risks agreed by the parties and may allow a contractor a means of escaping from an otherwise loss-making contract. This is a decision of Australia's highest court and is likely to encourage arguments for change in other jurisdictions.

Mann v Paterson Constructions Pty Ltd

Paterson Constructions (the "Contractor" in this case) was contracted to construct two townhouses on the Manns' property in Victoria, Australia. As a result of various matters arising during the project, including the Contractor's failure to complete and handover the works to the Manns by the due date set out in the contract, the Manns considered the Contractor to have repudiated the agreement, purported to accept that repudiation and terminated the contract. The Contractor considered this termination to be unlawful and of itself an act of repudiation, which it accepted. On this basis, the Contractor advanced claims against the Manns on a quantum meruit basis.

The Victorian Civil and Administrative Tribunal ("VCAT") found that the Contractor was not liable for the delay that resulted in its failure to complete the works by the due date, and determined that the Manns had repudiated the contract by their purported acceptance of the Contractor's alleged repudiation and their subsequent termination. VCAT ordered the Manns to pay the Contractor's losses on a quantum meruit basis. VCAT noted that the effect of this was that the Contractor was able to recover an amount well in excess of what it would have been entitled to under the contract.

The Manns unsuccessfully appealed to the Supreme Court of Victoria and the Victorian Court of Appeal, which both upheld the entitlement to claim on a quantum meruit basis and VCAT's valuation of the Contractor's losses (save for a minor mathematical correction). Pursuant to a grant of special leave to appeal, the Manns further appealed to the High Court of Australia, Australia's highest court.

The traditional position revised

It has long been the position that an innocent party may elect to claim on a quantum meruit basis (i.e. the reasonable value of work performed) as an alternative to claiming for damages in the wake of a termination for repudiation. That proposition was confirmed by the Judicial Committee of the Privy Council (comprised of judges from the UK's highest court) in *Lodder v Slowey* on the basis that once terminated for repudiation the relevant contract had been rescinded ab initio, as if it never existed. The contractor was therefore entitled to recover a sum assessed as the reasonable value of the services rendered, even though the amount so assessed might substantially exceed the agreed price. At Court of Appeal stage, Williams J explained: *"As the defendant has abandoned the special contract, and as the plaintiff has accepted that abandonment, what would have happened if the special contract had continued in existence is entirely irrelevant."* This proposition was subsequently accepted in most Australian jurisdictions, as well as many other jurisdictions internationally.

In upholding the Manns' appeal in the present case, the Australian High Court held that "the theory that the contract between the parties becomes 'entirely irrelevant' upon discharge for repudiation or breach is indeed fallacious" (the "recission fallacy"). The court relied upon a number of authorities which show that the termination of a contract for repudiation or breach does not result in a contract being void ab initio, but only that the parties are discharged from future performance. These authorities had been decided after *Lodder v Slowey*, but that case had continued to be applied. The Australian High Court also relied upon the following further points as the basis for its decision:

- The recission fallacy incorrectly denies the basic principle that the effect of the acceptance of a repudiation is that the innocent party is only absolved from future performance of its obligations under the contract. It does not alter or replace the accrued rights and obligations arising under the contract prior to the date of termination. Accordingly, the loss that the contractor is entitled to recover in the event of such termination is in effect a "loss of bargain", which is "*no less a creature of the contract than the right to recover sums that become due before its termination*". It follows that the terms of the terminated contract must inform the quantum of damages recoverable. To suggest otherwise would expand the law of restitution to redistribute risks for which provision has been made under an applicable contract and "*undermine the parties' bargain as to the allocation of risks and quantification of liabilities, and so undermine the abiding values of individual autonomy and freedom of contract"*.
- In circumstances where the respondent has enforceable contractual rights to money that have become due under the contract, there is no room for a right to elect to claim a reasonable remuneration unconstrained by the contract between the parties. To allow a restitutionary claim in these circumstances would be to subvert the contractual allocation of risk and may result in a windfall that is inconsistent with the contract whereby the parties' commercial risks were allocated between them and their liabilities limited (including in relation to price).
- Where a contractual entitlement to payment had not yet accrued for works carried out by the contractor prior to termination (e.g. where the obligations under the contract were entire), a bare majority of the court held that non-contractual quantum meruit claims were permissible but that the agreed contract price operates as a cap on the contractor's entitlement. The contract price agreed to by the parties for the performance of the work (or that part of it which relates to the claim in question) is to be regarded as the greatest possible remuneration for the work even on a quantum meruit basis.

Whilst this decision does not entirely remove the availability of quantum meruit claims in repudiation scenarios, it does significantly narrow their scope (namely, in respect of works for which a contractual entitlement has not yet accrued) and the maximum sum of losses that will be claimable (namely, by reference to the contract price).

Conclusions and implications

This is one of the first decisions internationally to significantly depart from a substantial body of accepted common law jurisprudence regarding the availability of quantum meruit claims arising from the repudiation of a construction contract, and in doing so, grants credence to the long stream of judicial and non-judicial criticism of the traditional position. The traditional position had provided a potential loophole for contractors to overcome loss-making contracts, by provoking the owner/employer to terminate in the hope that any ambiguity over the validity of the termination would allow a credible case to be made as to repudiation and the bringing of a quantum meruit claim considerably in excess of the contract price. This decision will give greater comfort to owners/employers (in Australia) that the risks of pursuing termination in such circumstances are much reduced.

One issue left unclear by the High Court's decision is the extent to which ordinary interim payment provisions will prevent the making of quantum meruit claims. The contract before the court contained staged payments referable to specific portions of work, rather than "one entire obligation to complete the whole of the contract works in order to become entitled to payment of an indivisible contract price". The position might well be different for interim payments made on a periodic basis by reference to the value of the works and expressly stated to be "on account". There may also be complexities insofar as claims include works which the contractor alleges arose as a result of variations which have not been formally approved/accepted by the employer prior to termination.

However, the potential for large quantum meruit claims to be made in relation to entire contracts, and to a lesser extent in relation to indivisible parts of non-entire contracts, will now be significantly tempered by the court's finding that the contract price imposes a ceiling on the quantum of any claim. The same may be said in respect of disputed variation claims, since contractors will now need to invest significant efforts in evidencing any adjustment to the contract sum, as opposed to simply evidencing the value of work it has carried out (as identified by Gageler J, "*a non-contractual quantum meruit has the advantage that proof of the value of services rendered is almost invariably more straightforward than proof of contractual loss.*")

As noted above, the traditional position overturned by this decision is mirrored in a number of jurisdictions (including England) and has similarly been criticised in these jurisdictions. It is likely that this decision will provide persuasive support of such criticisms when similar cases come before the courts of other jurisdictions, potentially resulting in similar changes to those favoured by the Australian High Court.

References: *Lodder v Slowey* [1904] AC 442; *Mann v Paterson Constructions Pty Ltd* [2019] HCA 32

Paying subcontractors directly

An English Commercial Court decision last year has considered the ability of an employer to recover payments made directly to subcontractors from its main contractor. The decision raises interesting questions as to the extent to which an employer must prove liability as between the main contractor and subcontractor in order to succeed in recovering such payments. The decision will be of considerable interest to employers faced with deteriorating commercial relationships at subcontract level and who are considering proactive steps by way of direct payment to avoid potential disruption through subcontractor suspension or termination scenarios.

Introduction

Employers can sometimes find themselves wishing to make direct payments to subcontractors engaged by their main contractor. This might be the case if a payment dispute arises at subcontract level or if the main contractor suffers cashflow difficulties. Subcontractors may threaten to terminate or suspend work in such circumstances and the employer may feel that direct payments are necessary to keep the project afloat.

Although the commercial rationale for such payments is clear, they pose a number of legal issues. The employer will usually wish to recover such payments from the main contractor and may initially seek to set them off against amounts due under the main contract. However, the main contractor is likely to put the employer to proof as to those set-offs and the employer will usually know very little about any disputed claims at subcontract level. It may therefore struggle to prove that the main contractor was liable to pay such sums to the subcontractor. The employer might consider taking an assignment of the subcontractor's claims and requiring it to lend such assistance as may be required in the proving of those claims against the main contractor. However, the subcontractor may be unwilling to provide such assistance or may not do so in a sufficiently timely or fulsome way.

If the employer's attempt at reimbursement from the main contractor fails, the employer may wish to reclaim the sums paid back from the subcontractor. The subcontractor may resist such attempts and/or may be unable to repay such sums in the absence of any security taken by the employer.

Cases dealing with these issues are rare, however, a recent arbitration appeal heard by the English Commercial Court provides a good illustration of the legal difficulties faced by employers in such circumstances and potential routes to overcome them.

Nobiskrug GmbH v Valla Yachts Ltd

Valla Yachts engaged Nobiskrug, a German shipyard, to build a superyacht – one of the largest private sailing vessels in the world. The contract between the parties did not contain provisions governing direct payments, but during the course of the project, Valla Yachts made a number of payments to certain nominated subcontractors who had brought claims against Nobiskrug. Nobiskrug contested most of these claims and the subcontractors had threatened to cease work. Valla Yachts wished to avoid this result, and the considerable disruption it would entail, and when making the payments expressly reserved its right to recover them from Nobiskrug.

Valla Yachts subsequently commenced arbitration proceedings against Nobiskrug to recover the payments. Among other things, it claimed that Nobiskrug had breached certain co-ordination and project management obligations contained in the main contract, which required Nobiskrug to manage and investigate claims made against it by the specialist subcontractors.

The arbitral tribunal emphasised the reservation of rights made by Valla Yachts, but its award was unclear as to whether the payments could be recovered without proving that Nobiskrug was obliged to make those payments to the subcontractors. Valla Yachts had not been able to submit evidence to the tribunal proving such an obligation.

The tribunal nevertheless accepted Valla Yachts' case as to project management failings. The tribunal held that Nobiskrug had effectively abandoned its project management responsibilities. That had caused the subcontractor claims to escalate and had placed Valla Yachts in an "*extremely difficult position*", given that the subcontractors in question were critical for the completion of the works. However, Valla Yachts would only be entitled to damages for such breaches if they "*were an effective cause*" of the additional costs claimed by the subcontractors. The tribunal did not go on to determine that issue, but nonetheless ordered Nobiskrug to reimburse certain of the payments made by Valla Yachts on grounds which were not clear from the award.

Appeal to the Commercial Court

Nobiskrug appealed the tribunal's decision, asserting that the tribunal had made an error in finding that it should reimburse Valla Yachts when there had been no finding that it was under a legal liability to the subcontractors in respect of the payments. Nobiskrug accepted there was a reservation of rights but argued that this did not create a right or a cause of action against Nobiskrug for the recovery of sums paid to the subcontractors. Nobiskrug's position was that the payments made by Valla Yachts were voluntary and the reservation of rights simply meant that Valla Yachts had not waived its right to recover the monies by pursuing its counterclaims.

Valla Yachts argued that the tribunal's award could be supported on restitutionary grounds, as follows:

- The tribunal had found that Nobiskrug had abrogated its project management responsibilities and had failed (i) to investigate the claims advanced so that Valla Yachts was unable to form a proper assessment of whether the payments demanded were due and (ii) to manage their resolution effectively so as to minimize any disruption caused to the works.
- These breaches had placed Valla Yachts in an extremely difficult position where it was compelled to make the payments if the yacht was to be completed.
- Its action in making the payments was to the benefit of Nobiskrug in that it was discharging Nobiskrug's project management responsibilities, or at least mitigating the breach of those responsibilities. Payment allowed the project to continue and Nobiskrug to earn the contract price. Therefore, Nobiskrug was unjustly enriched and Valla Yachts had a valid restitutionary claim.

Somewhat inevitably, the Commercial Court remitted the matter to the tribunal for further consideration. The Court did not think the tribunal could be said to have ordered the reimbursement of payments made by Valla Yachts "*simply on the basis that it made them subject to a reservation of rights*". On the other hand, it was unclear on what basis the tribunal had ordered reimbursement and Valla Yachts restitutionary analysis was "*not spelt out completely on the face of the Award*". Of note, however, the Court considered that the restitutionary claim had "*considerable force*".

A restitutionary solution?

It will be unsurprising to most that a mere reservation of rights was insufficient to entitle the employer to the reimbursement of direct payments. Of much greater interest, however, is the Court's encouragement of a restitutionary claim based on the contractor's failure to adequately manage subcontractor claims. If successful, such an argument would appear to avoid the need for the employer to prove that (i) the contractor had a liability to the subcontractors in respect of the amounts paid by the employer; or (ii) the contractor's project management failings had caused or contributed to the amounts claimed by the subcontractors. The ability to make such claims would be of considerable assistance to employers finding themselves in a similar position to Valla Yachts.

The restitutionary argument is not without difficulty, however. Such claims are usually unavailable where contractual remedies already exist. It might be said that the employer should be left to its usual remedy to sue the contractor for damages caused by a breach of any project management obligations. A restitutionary claim, if successful, may also work considerable injustice to the main contractor. Having reimbursed the employer for payments made directly to its subcontractors, it may find itself without any ability to recover those amounts. Even if it were to subsequently show that the subcontractors' claims were invalid, it is difficult to immediately identify what cause of action would be available to it to claim for the reimbursement of the sums it had paid to the Employer.

Contractual solutions

Express contractual provisions provide another potential solution. In the FIDIC First Editions, the Red Book and MDB contracts provide for a right for the Employer to pay Nominated Subcontractors directly (Clause 5.4 in both). This right has now been extended to the Yellow and Silver Books in the FIDIC Second Edition (Clause 4.5 in both). The right is limited, however, to Nominated Subcontractor payments previously included within Payment Certificates which have been paid to the Contractor and which the Contractor has no right to withhold from the Nominated Subcontractor. The provisions are therefore aimed at a situation where:

— a Contractor has included a payment to a Nominated Subcontractor within its payment application; and

— those payments have been included within the Employer's Payment Certificate and paid to the Contractor; but

— the Contractor has failed to pay those amounts over to the Nominated Subcontractor; and

— has not satisfied the Engineer and/or Employer that "*the Contractor is reasonably entitled to withhold or refuse to pay these amounts*".

Such cases of blatant "cashflow hoarding" are likely to be less common than cases involving disputed entitlements between the Contractor and its subcontractors. For example, the Contractor may seek to withhold payment to the subcontractor on account of deductions for delay or defects. Alternatively, as was the case in Valla Yachts, the Contractor may dispute the subcontractor's right to payment altogether and not have included it in its application for payment to the Employer. This is likely to occur where, as in Valla Yachts, the subcontractor makes claims for compensation as a result of disruption for which the Contractor is said to be responsible.

Such situations are less susceptible to contractual solutions ahead of time. Any contractual right for the Employer to pay directly and recover those payments from the Contractor will prejudice the Contractor's rights against the subcontractor and are unlikely to be acceptable. Solutions which are more process-driven may find agreement, however. For example, the Employer might be given the right to withhold payment whilst a period of mandatory alternative dispute resolution is pursued between the Contractor and subcontractor (with or without the Employer). Alternatively, payment might be held by the Employer pending dispute adjudication under the subcontract (whether under local law procedures or under something akin to the FIDIC Dispute Avoidance and Adjudication Board).

Whether such contractual solutions are pursued or the issue is left to be dealt with on an ad-hoc basis, the question of direct payments arises with sufficient frequency to merit serious consideration by employers prior to entry into a construction contract.

References: *Nobiskrug GmbH v Valla Yachts Ltd* [2019] EWHC 1219 (Comm).

FIDIC Second Edition claims notification provisions

A decision of the Supreme Court (the UK's highest court) last year has reversed two Court of Appeal decisions in 2016 which had significantly diluted the effect of "anti-variation" and "no-waiver" provisions. The Supreme Court has ruled that such clauses are effective to bind the parties as to the mode by which subsequent variations or waivers must be made. This decision has particular relevance for construction projects where variations and other agreements or waivers are often discussed informally among the project teams for each party.

FIDIC Second Edition Claims Procedure

The FIDIC Second Edition contracts released in late 2017 contained significant revisions to their standard claims notification procedure. For a full analysis of the revised procedure, please see our 2018 *Annual Review*. A summary of those aspects of the procedure relevant for present purposes follows below:

— Both the Employer and Contractor must notify Claims for additional payment or extensions of time to the Engineer within 28 days of becoming aware, or when they should have become aware, of the event or circumstance giving rise to the Claim (the "Trigger Date"). A failure to notify within this period renders the Claim liable to be barred and the receiving party discharged from any liability.

— If the Engineer (or the receiving Party under the Silver Book) believes that such a Claim has been notified late and is barred, it must serve a notice to this effect (the "First Barring Notice") within 14 days of receiving the Notice of Claim. In the absence of such a notice, the Notice of Claim is deemed to be valid.

— A fully detailed Claim is then required within 84 days of the Trigger Date. The fully detailed Claim should contain, in summary:

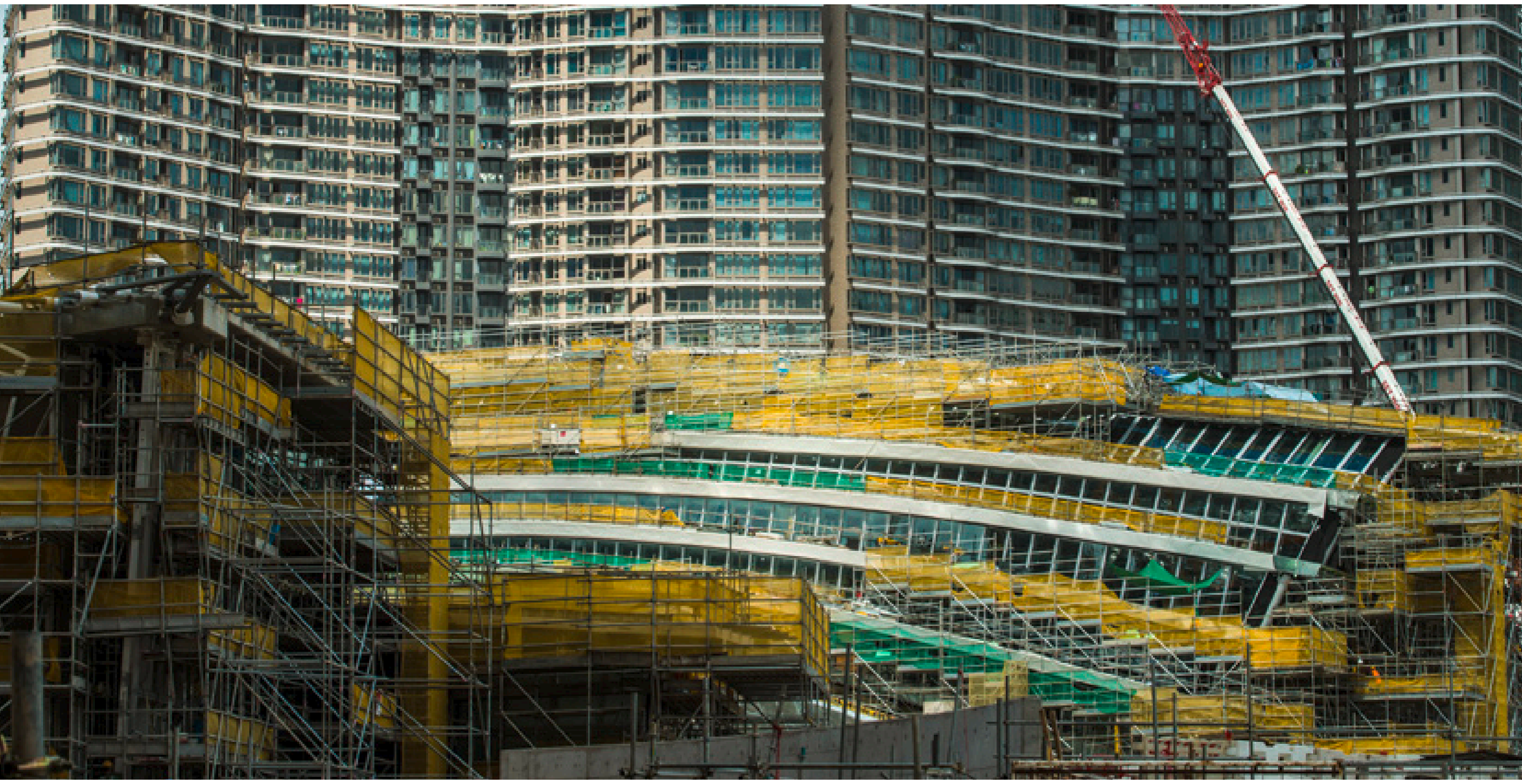
- a detailed description of the event or circumstance giving rise to the Claim;
- a statement of the contractual and/or other legal basis of the Claim (the "Statement of Legal Basis");
- all contemporaneous records (which is a term now defined within clause 20) on which the claiming Party relies; and
- detailed supporting particulars of the amount/EOT claimed.

— Failure to provide the Statement of Legal Basis within the 84 day time period (but not any of the other items listed above) renders the Claim liable to be barred and the receiving Party discharged from liability.

— If the Engineer (or Employer's Representative under the Silver Book) believes that the Statement of Legal Basis has not been given in time, he or she must serve a notice to this effect (the "Second Barring Notice") within 14 days of the expiry of the 84-day period. In the absence of such a notice, the Notice of Claim is deemed to be valid.

— Both the claiming Party and the receiving Party are given the ability to dispute the First or Second Barring Notice or the absence of those notices as the case may be (and similarly in relation to barring notices issued by the receiving Party or the Employer's Representative under the Silver Book). The Engineer/Employer's Representative must then include a review as to whether the Claim is barred in his determination of the Claim. The Engineer's/Employer's Representative's review in this regard is not limited to matters of timing but may also consider whether a late submission is justified on broader grounds such as the absence of prejudice and prior knowledge of the Claim by the receiving Party.

— Once the fully detailed Claim has been submitted, provision is made for the Engineer/Employer's Representative to consult with both Parties and in the absence of agreement to reach a determination of the Claim. Either Party may then issue a Notice of Dissatisfaction and refer the Claim to the Dispute Avoidance and Adjudication Board ("DAAB") and then ultimately to arbitration.



A claiming Party must therefore submit its Statement of Legal Basis within 84 days, otherwise the Claim is liable to become barred. It need not submit its fully detailed Claim within this period, however. The Statement of Legal Basis is only one of four requirements for the fully detailed Claim, which is also to include all contemporary records on which the claiming Party relies as well as a detailed quantum submission.

It is unclear whether the Contractor's Statement of Legal Basis is intended to limit the scope of any subsequent referral to the DAAB and thereafter to arbitration. The procedure does, however, require the Engineer (or Employer under the Silver Book) to determine the Claim as put forward in the Contractor's two notices. It is this determination which is then to be referred to the DAAB and then to arbitration. It may be open for the Employer to argue that any new legal basis for the claim is either time barred or must first be the subject of a further round of notices and a determination by the Engineer / Employer as to whether delay in submitting those notices is to be excused. Very similar issues were considered in a recent case arising from the construction of the Hong Kong to Guangzhou Express Rail Link connecting Hong Kong to mainland China.

Maeda Corporation v Bauer Hong Kong Ltd

Maeda Corporation ("Maeda") was appointed Main Contractor for the tunnelling aspects of the Hong Kong to Guangzhou Express Rail Link connecting Hong Kong to mainland China. Maeda subcontracted certain diaphragm wall work to Bauer Hong Kong Ltd ("Bauer"). During the course of the works, Bauer encountered unforeseen ground conditions and claimed additional payment from Maeda. Bauer initially claimed that the additional work required to overcome the conditions amounted to a variation under the subcontract. By the time the claim had reached arbitration, Bauer had expanded its grounds of claim to an unforeseen ground conditions clause in the subcontract as well the variation clause.

The claims notification provision under the subcontract required Bauer to give a notice of claim within 14 days of the event, occurrence or matter giving rise to the claim. A further notice, described as a condition precedent to entitlement, was to be given 28 days later setting out the "*contractual basis together with full and detailed particulars and the evaluation of the claim*". The subcontract also made clear that Bauer would have no right to any additional payment unless the claims notification procedure had been "*strictly complied with*".

It was common ground that Bauer's initial notices of claim only referred to the variation provisions of the subcontract. Maeda argued that Bauer's claim under the unforeseen ground conditions clause was therefore barred. The arbitrator rejected this challenge, noting that it was unrealistic to expect a party to finalise its legal case within the periods provided for notification of a claim. It was sufficient in his view for the factual basis of a claim to be communicated. As the arbitrator had rejected Bauer's case under the variation clause, this finding was crucial to the success of Bauer's claim (under the unforeseen ground conditions clause).

The Hong Kong High Court overturned the arbitrator's decision on this issue. Given the notice provisions were to be strictly complied with and were expressly designated as conditions precedent, Bauer's initial notices limiting the contractual basis of its claim to the variation provision were binding. As such, Bauer "*should have no right to the additional extra payment, loss and expense claimed*" under the unforeseen ground conditions clause. As regards any unfairness in requiring Bauer to finalise its legal case within the short period required by the notification provisions:

> *"[Bauer] had 42 days from the event or occurrence giving rise to the claim to serve the notice required under Clause 21.2. That is not an unrealistic timeframe to identify the contractual basis of a claim."*

Parallels with the FIDIC Second Edition

There are evident parallels between this case and the claims notification procedure under the FIDIC Second Edition. Both require a second notice setting out the contractual or legal basis for a claim. Both also contain language barring claims which do not comply with this requirement. The FIDIC procedure permits non-compliance to be excused in certain circumstances, but the decision in this case would appear to remain relevant in circumstances where any non-compliance is not excused.

One argument which does not appear to have been considered by the arbitrator or the Hong Kong court is why the second notice should need to set out an exhaustive statement of legal basis. Provided that a legal basis is stated, it might be argued that the requirements of the notice provision have been satisfied and need not impose any restriction on broadening the legal basis at a later date. On the other hand, the close linkage in the FIDIC procedure between the notices of claim, the subsequent determination by the Engineer / Employer, and the referral of that determination to the DAAB or to arbitration, may provide arguments in support of a stricter interpretation.

Also of relevance is a comparison with the FIDIC Gold Book from which the claims notification provisions of the FIDIC Second Editions were developed. The Gold Book Claims provision requires a "*fully detailed claim which includes full supporting particulars of the contractual or other basis of the claim*". The claim is to be barred if the Contractor fails to "*provide the contractual or other basis of the claim within the said 42 days*". This contrasts with the First Edition of the Yellow, Red and Silver books which simply require a "*fully detailed claim which includes full supporting particulars of the basis of the claim*" and include no time-bar.

The Gold Book reference to "*full supporting particulars of the contractual or other basis of the claim*" might be thought to refer to something similar to a fully detailed claim (i.e. either because "other basis" could include factual matters or because full supporting particulars of the contractual basis would require a statement of facts). Such an interpretation is not possible for the new Second Editions because there is now a list of four separate requirements for a fully detailed Claim, one of which is described as the "*contractual and/or other legal basis of the Claim*". This is the only element to which the time bar attaches and refers only to the "legal" basis of the Claim.

The singling out of the Statement of Legal Basis in this way might be said to emphasis the reasoning adopted by Hong Kong High Court. The fact that only the Statement of Legal Basis attracts a time bar could be said to be an indication that the claiming party was to be bound by that statement in contrast to the other three elements of the fully detailed Claim which are all evidential in nature.

Given that notices of claim are often submitted by project teams without legal input, the drafting of imprecise or mistaken Statements of Legal Basis is likely to arise with frequency on projects let under the FIDIC Second Edition forms. As we noted after the release of the new edition, parties will need to be well prepared and adequately resourced to manage the new provisions. Those who are not may find that entitlements have been unwittingly lost.

References: *Maeda Corporation v Bauer Hong Kong Ltd* [2019] HKCFI 916

Delay analysis methodologies

A decision of an Australian court last year has considered the evidential requirements for proving delay claims in construction disputes. The decision comments on the relevance of the 2nd Edition of the SCL Delay and Disruption Protocol and on two popular delay analysis methodologies contained in the Protocol. In the circumstances of this case, the court ultimately rejected both methodologies and preferred a broad common sense approach paying close attention to the facts. The court's approach is likely to be relevant to construction disputes elsewhere in the world where these methodologies are deployed.

Delay analysis and the SCL Protocol

The SCL Delay and Disruption Protocol (the "Protocol") is a document published by the Society of Construction Law (now in its 2nd Edition) which has as its object to "*provide useful guidance on some of the common delay and disruption issues that arise on construction projects*". Among other things, the Protocol sets out six commonly used forms of delay analysis in construction disputes, together with certain criteria it recommends be applied to determine the most suitable method.

Two popular methods of delay analysis referred to in the Protocol are "As-Planned v As-Built Windows Analysis" and "Collapsed As-Built Analysis". In the former, certain chunks of time or "windows" are taken (usually based on milestones or fixed periods of time) and as-planned and as-built programme records are considered to identify the critical path during the relevant window and the amount of delay it incurred. This delay is then sought to be attributed to causes during the period through a close review of the project records.

The Collapsed As-Built Analysis requires a detailed logic-linked as-built programme. Once this has been developed, the programme is "collapsed" by identifying delaying events and removing them from the programme to provide a hypothesis as to the delay caused by those events. The use of programming software allows the as-built programme to be easily probed in this way to provide an assessment of the way in which the works would have proceeded had certain delay events not occurred. The method is heavily dependent on the logic-links included when preparing the as-built programme.

Both of these methods were considered by the Australian decision discussed below.

White Constructions Pty Ltd v PBS Holdings Pty Ltd

White was the developer of a housing development in Kiama, just south of Sydney in Australia. It engaged Illawarra Water & Sewer Design Pty Ltd ("IWS") as sewer designer for the development. Considerable delay was suffered in having IWS's sewer design approved by Sydney Water (the relevant public authority). White alleged that IWS's original design had been flawed and that the resulting delays in obtaining approval for a revised design caused a knock-on delays to the development as a whole of more than 7 months.

White submitted evidence from a delay expert, which supported its delay case and relied on an As-Planned v As-Built Windows Analysis. IWS submitted a report from a delay expert claiming that, at most, only 19 days of delay were caused. IWS's expert relied on a Collapsed As-Built Analysis. Both of the experts criticised the other's choice of methodology.

The New South Wales Supreme Court accepted the criticisms made by both experts as to the others' approach. Some of the key criticisms were:

- That the logic-links in the as-built programme prepared by IWS's expert were not sustainable.
- That IWS's Collapsed As-Built Analysis was too simplistic and obscured the inefficient performance of work caused by the delayed sewer approvals.
- The Windows Analysis prepared by White's expert had not taken into account certain delays un-related to the sewer design and had assumed unjustifiable as-built logic links.
- The Windows Analysis was also flawed because it "*assumes causation rather than identifies actual evidence of it*".

Justice Hammerschlag opined that while both experts were adept at their art, both could not be right and it was not inevitable that one of them was right. The court therefore rejected the evidence of both experts and proceeded to appoint its own expert. On the advice of that expert, the approach favoured by the court was an open-textured one, unbounded by any specific methodology. The court considered that:

> *"close consideration and examination of the actual evidence of what was happening on the ground will reveal if the delay in approving the sewerage design actually played a role in delaying the project and, if so, how and by how much. … the Court should apply the common law common sense approach to causation … The only appropriate method is to determine the matter by paying close attention to the facts, and assessing whether White has proved, on the probabilities, that delay in the [sewer design] delayed the project as a whole and, if so, by how much."*

The court also declined to give any special standing to the delay analysis methodologies included within the Protocol: "for the purpose of any particular case, the fact that a method appears in the Protocol does not give it any standing, and the fact that a method, which is otherwise logical or rational, but does not appear in the Protocol, does not deny it standing."

Applying the court's common sense approach to the delay issues, White's delay case was dismissed on the basis that significant gaps in the evidence existed, meaning there was insufficient proof of the specific delaying effects of the revised sewer design.

Conclusions and implications

Although of limited effect as a legal precedent (even in Australia because of the structure of the Australian legal system), the comments made in this case as to the two delay analysis methodologies referred to, as well as the common sense approach preferred by the court, are likely to be highly persuasive in other Australian jurisdictions and of broader relevance to construction disputes elsewhere in the world. Some of the criticisms made of those methodologies could be said to be of general application, while others may be the result of poor records. The overall impression from the judgment is that the court considered each of the experts to be advancing methodology at the expense of evidence.

There is some support for the court's common sense approach in the SCL Protocol itself. Paragraph 11.2 notes that: "*Irrespective of which method of delay analysis is deployed, there is an overriding objective of ensuring that the conclusions derived from that analysis are sound from a common sense perspective*."

The court's decision also highlights the importance of delay experts attempting to agree on an appropriate methodology at the outset. Although differences in methodology can favour one parties' case over another, disagreement over methodology can prove extremely wasteful. Debates over methodology can take on a life of their own and distract from a focus on important factual issues. The court in this case felt unable to support either of the positions adopted and was forced to do its best with a broad common sense approach.

References: *White Constructions Pty Ltd v PBS Holdings Pty Ltd* [2019] NSWSC 1166.

Investment arbitration and construction contracts: jurisdiction over ancillary agreements and EDF funded projects

A recent ICSID tribunal has upheld jurisdiction over a dispute concerning an alleged settlement agreement arising from contractor claims on a major infrastructure project in the Republic of Mozambique. In addition to deciding that its jurisdiction extended to such ancillary agreements, the tribunal rejected an argument that its jurisdiction was limited by a purported exclusive jurisdiction mechanism for projects funded by the European Development Fund, which provides that any disputes arising from such projects shall be determined pursuant to the dispute resolution mechanism set out in the Cotonou Convention.

CMC Muratori Cementisti CMC Di Ravenna Società Cooperativa v Mozambique

Mozambique's main road (the 'N1') runs from Maputo in the south to Pemba in the north. Following a decision by the Government to rehabilitate a significant stretch of this road, the "Namacurra-Rio Ligonha Project" was born. The Ministry of Public Works and Housing (the "Ministry"), who was responsible for these works, delegated responsibility to deliver the Project to the Administracão Nacional de Estradas ("ANE"). Following a public tender process, in 2005 ANE awarded to CMC a contract for works in relation to the Lot 3 of the Project (the "Contract"). The works were funded by the European Development Fund ("EDF").

CMC carried out the works between 2005 and 2008. During the course of these works, CMC alleged that it carried out various additional works and suffered delay and disruption, for which it was entitled to additional compensation. During 2009, the parties exchanged various correspondence through which ANE made a commercial offer to pay a sum to CMC in satisfaction of these claims. A dispute arose between the parties as to whether CMC's response to this offer constituted an acceptance of the proposal or a counter-offer (the "Settlement Agreement"). In any event, ANE never made payment of the proposed sum to CMC and, following a change in Government officials in charge of the Ministry and ANE, ANE refused to make payment of the proposed sum and sought to resile from its original offer.

In 2017, CMC initiated proceedings under the ICSID Convention against the Republic of Mozambique to recover its alleged entitlement to additional compensation. CMC relied on a bilateral investment treaty (the "BIT") between Mozambique and Italy (where the CMC group of companies was based). In response, Mozambique raised a number of jurisdictional objections. In an award handed down in October 2019, the tribunal dismissed Mozambique's jurisdictional objections and further dismissed CMC's claim on the merits. For the purpose of this article, we focus on Mozambique's jurisdictional objections.

Is a 'settlement agreement' an investment?

The scope of the dispute largely concerned the validity of the alleged Settlement Agreement. Whilst it is well-established that a contract for construction works is an investment for the purposes of the ICSID Convention, Mozambique argued that the Tribunal did not have jurisdiction because the alleged Settlement Agreement was merely a "*legal act*" and, of itself, involved no contribution to, or relevant economic activity within, Mozambique (as required by the ICISD Convention).

In response, CMC argued that the Settlement Agreement was either itself an investment in Mozambique, or that it was at the least a "*credit for sums of money or any performance having economic value connected with an investment*", part of the definition of 'investment' set out in the applicable BIT.

CMC also argued that the alleged Settlement Agreement was an investment by virtue of the fact that it was connected to and arose from the Contract, thereby making it both an "*associated activity*" and "*performance having economic value connected with an investment" under the definition of 'investment*'.

In considering whether the Settlement Agreement was an investment under the ICSID Convention, the tribunal weighed up a number of authorities and applied an approach of determining whether the definition of 'investment' in the BIT "*exceeds what is permissible*" under the ICSID Convention. The tribunal ruled in favour of CMC finding that "the definition of "investment" in the [investment treaty] does not exceed what is permissible under the ICSID Convention. The Claimants' claims "*for sums of money or any performance having an economic value" within the meaning of Article 1(c) of the [investment treaty] arise directly out of their investment in the Lot 3 Project. In the view of the Tribunal, that is sufficient to bring the Claimants' claims within the jurisdiction of the Tribunal under both the [investment treaty] and the ICSID Convention*".

ICSID Jurisdiction for EDF Funded Projects

Mozambique and Italy are both parties to the *Partnership Agreement between the members of the African, Caribbean and Pacific Group of States, of the one part, and the European Community and its Member States, of the other part* (the "Cotonou Convention"). As a matter of standard practice, construction contracts for EDF funded projects typically adopt a standard form dispute resolution provision that, in the case of 'transnational contracts', disputes shall be settled either (a) in accordance with the national legislation of the State of the Contracting Authority or its established practices, if the parties so agree; or (b) by Cotonou Convention arbitration. Mozambique argued that the only dispute resolution option was Cotonou Convention arbitration (and not ICSID arbitration). Mozambique advanced a number of arguments in this regard, including that:

(i) the dispute around the validity and enforceability of the alleged Settlement Agreement related to the Contract and was therefore captured by the dispute resolution provisions in the Contract;

(ii) since the parties had not agreed otherwise, the dispute resolution provisions in the Contract provided for arbitration pursuant to the Cotonou Arbitration Rules; and

(iii) under the Cotonou Convention, the use of other arbitration rules is excluded and therefore ICSID does not have jurisdiction. Mozambique also noted that arbitration of this dispute pursuant to the Cotonou Arbitration Rules would be consistent with the BIT which permits a dispute under the treaty to be submitted to "*other international arbitration arrangements, mechanisms, or instruments,*" as an alternative to the ICSID Rules "*at the[e]choice*" of the parties. Therefore, CMC's agreement to the dispute provisions of the Contract was "*a clear waiver of ICSID jurisdiction*". Mozambique also cited Article 30 of Annex IV of the Cotonou Convention, which states that it applies to "*any dispute arising between the authorities of an ACP State and a contractor, supplier or provider of services during the performance of a contract financed by the Fund [EDF],*" and that those disputes "*shall*" be settled pursuant to the Cotonou Arbitration Rules.

The tribunal considered the impact of the Cotonou Convention both at a treaty level and at a contractual level:

— At a treaty level, the tribunal noted that Article 30 of Annex IV to the Convention applied only in respect of a dispute arising "during the performance" of the Contract. In the tribunal's view, because the dispute around the validity and enforceability of the Settlement Agreement arose after the completion of CMC's works, this was not a dispute arising 'during the performance of' the Contract.

— At a contractual level, whilst the parties had agreed to submit disputes arising under the Contract to arbitration under the Cotonou Arbitration Rules, the tribunal emphasised that the present claims were not merely claims for breach of contract. Rather, CMC's claims all concerned disputes arising under the BIT. As a result, the Contract provisions did not deprive the tribunal of jurisdiction.

Conclusion

This is an interesting decision insofar as it confirms that where the relevant provisions of the applicable investment treaty are sufficiently broad (as was the case here), there is sufficient scope for ICSID jurisdiction to extend to disputes arising from commercial agreements or issues that are incidental to, but not part of, a contract for construction works. Such types of agreements (which may include commercial agreements for the resolution of claims, advance payments, performance incentives or additional security) are not uncommon on construction projects. These contracts can often include little or no consideration, or may even simply be an affirmation of a commercial arrangement between the Parties. Despite the fact that the subject matter of these agreements may not satisfy the definition of an 'investment' for the purpose of the BIT or Article 25 of the ICSID Convention, this decision opens the door for disputes arising in relation to these ancillary agreements to be wrapped up in the claimant's original 'investment' construction contract, and subject to ICSID jurisdiction.

By contrast, the tribunal's findings in relation to the Cotonou Convention suggest that the dispute concerning the Settlement Agreement was not sufficiently connected to the works to be covered by the Cotonou Convention arbitration provisions. The tribunal's decision leaves unclear which forum would be most appropriate for the resolution of subsequent disputes arising "during the performance" of contracts financed under the framework of the Cotonou Convention. In those cases there would appear to be a conflict between the investment treaty and the Cotonou Convention. Although the Cotonou Convention was dated later than the investment treaty in the present case, the tribunal noted that arguments for the priority of the investment treaty might have been made based on the fact that the Cotonou Convention is the last in a serious of treaties (the tribunal did not need to determine this point).

Parties involved in EDF projects should also take careful note of the Tribunal's findings in relation to the dispute resolution provisions under the Contract. The Tribunal's judgment indicates that where parties seek to maintain exclusive jurisdiction for investment-treaty disputes under an alternative regime or to exclude ICSID jurisdiction in particular; clear, express and narrow language in the drafting of dispute resolution provisions is required.

References: *CMC Muratori Cementisti CMC Di Ravenna SOC. Coop., CMC MuratoriCementisti CMC Di Ravenna SOC. Coop. A.R.L. Maputo Branch and CMC Africa, and CMC Africa Austral, LDA v. Republic of Mozambique, ICSID* Case No. ARB/17/23.

Convention on the Settlement of Investment Disputes between States and Nationals of Other States dated 18 March 1965 (the "ICSID Convention").

Agreement between the Government of the Italian Republic and the Government of the Republic of Mozambique on the Promotion and Reciprocal Protection of Investments dated 14 December 1998 (the "BIT").

Partnership Agreement between the members of the African, Caribbean and Pacific Group of States, of the one part, and the European Community and its Member States, of the other part (the "Cotonou Convention").

Procedural Rules on Conciliation and Arbitration of contracts financed by the European Development Fund (the "Cotonou Arbitration Rules") as adopted by Decision No 3/90 on 29 March 1990.

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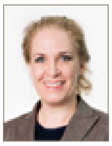

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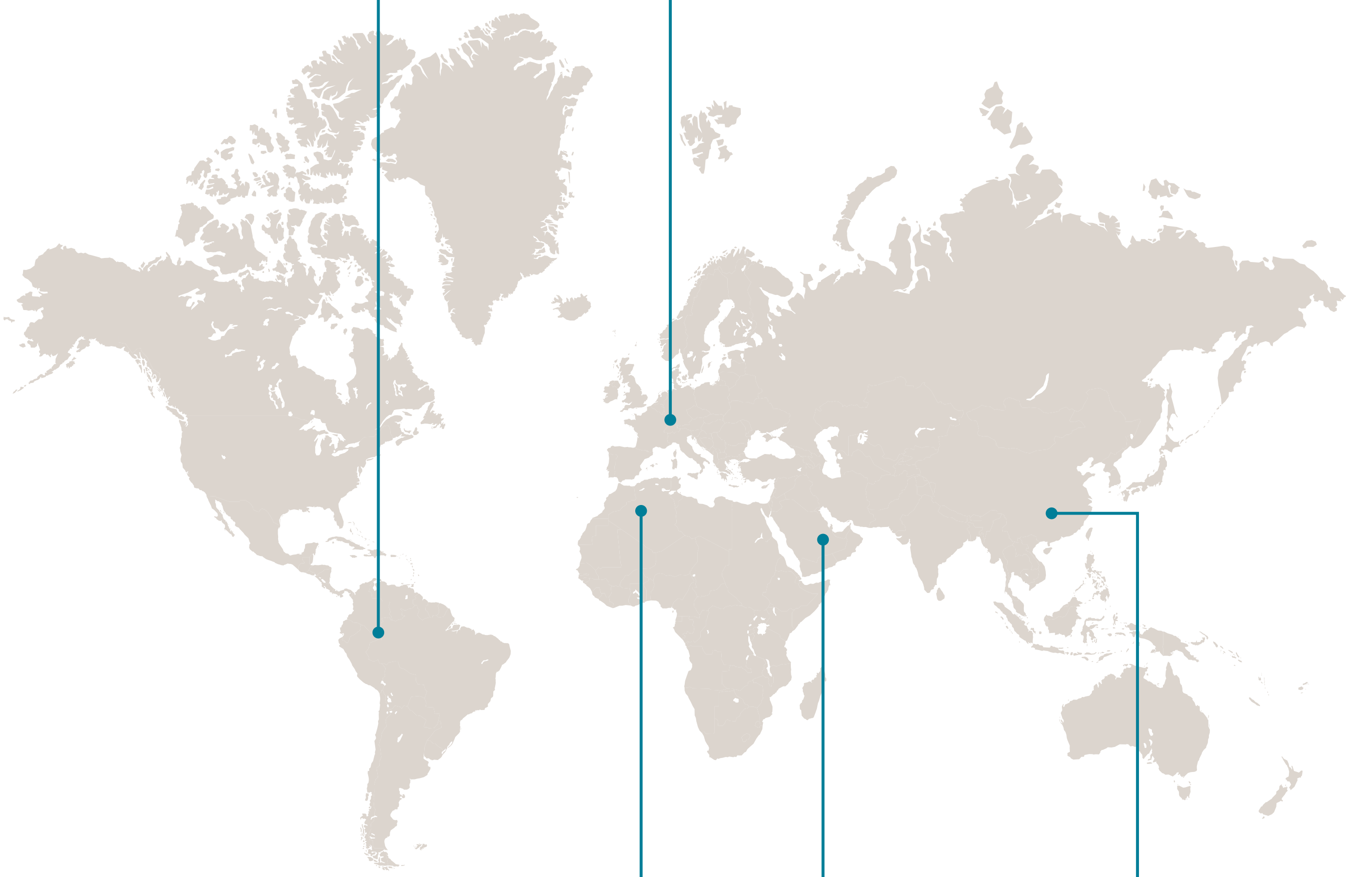

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