HFW

CONSTRUCTION BULLETIN
MARCH 2019

Welcome to the March edition of our Construction Bulletin.

In this edition we cover a broad range of recent developments in international construction law, as follows:

- Australia's Capital City Infrastructure Boom – Capacity and Capability Challenges
- Dispute Resolution in Kuwait
- Third Party Funding in Asia Pacific: An Update
- When Are Works 'Practically Complete'?

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

Ben Mellors, Partner, ben.mellors@hfw.com

ALEX MCKELLAR
PARTNER

"Strategically staging projects of significance to utilise resources efficiently will almost certainly reduce the drain on the taxpayer."

AUSTRALIA'S CAPITAL CITY INFRASTRUCTURE BOOM – CAPACITY AND CAPABILITY CHALLENGES

This article identifies capacity and capability challenges arising from the concurrent award of multiple major road and rail infrastructure projects in Australia's two largest cities and considers some of the responses to those challenges.

Introduction

The two largest cities in Australia, Sydney and Melbourne, are in the midst of an unprecedented infrastructure spending boom with in excess of AUS$20 billion being spent in the current financial year with similar projected expenditure in the next four financial years. A significant majority of that spending is allocated to road and rail projects in Sydney and Melbourne. The boom has created challenges for the building industry more broadly with capacity challenges in the supply of materials and a shortage of sufficiently experienced project management and administrative personnel.

Capacity

Capacity shortages are likely to be one of the great challenges of the boom given the long lead times which are often inherent in increasing capacity for the supply of materials and goods. This is particularly so when many of the projects are bid on the basis of minimum local content requirements.

One example is the lack of affordable sand especially in Sydney. Supply concerns with sand are not new in Sydney, or indeed globally, but the issue is particularly acute given the quantities required for the major civil works underway. To combat the challenge a facility in Glebe Island in the centre of Sydney capable of receiving sand barged from other locations such as Newcastle and Brisbane is proposed.

Capability

The major capability challenge created by the boom is a skills shortage. Skills shortages are particularly noticeable in project management and administration, but are expected to extend to specialised contracting services once the major civil works on many of the projects near completion.

As major projects have ramped up, the ability of all industry participants to employ skilled project managers and administrators has deteriorated. The primary impact of this shortage has been felt by the mid-tier of contractors, particularly in the high-rise residential and commercial construction sectors. That sector has already had to contend with significant tightening of credit, a corresponding reduction in available work, increasing developer contribution requirements and a significant fall in housing prices. Many of the projects now under construction were priced by contractors when conditions were far more benign. The lack of skilled managers and administrators, reduced ability to employ highly skilled subcontractors and the increased desire of financiers and developers to limit costs has led to numerous insolvencies with more likely to follow.

The capability issue has been brought to the fore recently by a group of nine Australian mid-tier construction companies known as Australian Owned Contractors (AOC) as part of a call for increased participation in major government projects. AOC is concerned by the extent of involvement of foreign-owned contractors. It says that this inhibits the ability of Australian contractors to build local expertise and experience in delivering major projects, along with a potential for lessening of market competition.

Lessons to be learned

Australia is a federation and there is often little dialogue between States particularly when States are represented by opposing political parties. Strategically staging projects of significance to utilise resources efficiently will almost certainly reduce the drain on the taxpayer. A more mature political dialogue and a better grasp of basic supply and demand economics would be a sound starting point for future infrastructure investment and timing decisions.

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DISPUTE RESOLUTION IN KUWAIT

Construction is booming in Kuwait and HFW is establishing a team in the country to meet demand. We recently acted for a contractor in Kuwait's highest court which confirmed that arbitration agreements will be respected and upheld.

New Kuwait 2035

As part of its New Kuwait 2035 plan Kuwait is entering a period of significant investment and development. Along with high profile mega-projects, including airports and causeways, Kuwait is modernising its utilities and infrastructure, expanding and improving its oil and gas facilities, and building hospitals, universities, cultural centres, solar parks, free trade zones and numerous housing, retail and leisure developments. To coincide with this period of rapid development HFW is expanding its office in Kuwait. I relocated to Kuwait earlier this year, to work more closely with our construction clients. It's an exciting time to be here.

Dispute resolution in Kuwait

The increased volume and sophistication of construction in Kuwait is attracting major international players. These contractors and consultants need to understand their options should disputes arise. Kuwait has been slower than other Gulf countries to embrace arbitration. Although arbitration agreements are relatively common in Kuwait, several state employers in Kuwait still currently insist on local courts as the only dispute resolution option in their contracts. The legal framework for arbitration in Kuwait is in need of reform. Whereas other Gulf countries have enacted arbitration laws based on the UNCITRAL Model Law, Kuwait is yet to do so. The current arbitration legislation is found in two separate laws – the Judicial Arbitration Law[1] and the Procedures Law[2] – both of which are unsuited to modern arbitration practice.

On a more positive note, Kuwait is a signatory to the New York Convention, allowing for enforcement of foreign awards in Kuwait and enforcement of awards made in Kuwait in other signatory countries. Also, recent local court cases confirmed that the Kuwaiti courts will respect and uphold parties' agreements to arbitrate.

Local courts uphold arbitration agreements

HFW recently acted for a contractor in a series of Kuwaiti court cases relating to the construction of a water distribution centre. Court proceedings were commenced by a local subcontractor, despite the subcontract containing an agreement to resolve all disputes by ICC arbitration in Singapore. In the Court of Cassation (Kuwait's highest court) HFW successfully argued that the Kuwaiti courts did not have jurisdiction to hear the subcontractor's claim, because the parties had agreed to arbitrate. The judgment, in October 2018, applied Article 173 of the Procedures Law under which the parties may agree in writing, in their original contract or a subsequent agreement, to submit their dispute to any arbitral procedure. The arbitration clause in the subcontract was held to remain effective, despite the subcontract having been terminated. This judgment followed a similar one in February 2018, in which the Court of Cassation found that an agreement to arbitrate in a distribution agreement excluded the jurisdiction of the Kuwaiti courts.

Comment

As Kuwait's development accelerates and the construction market becomes more sophisticated, it is important that all parties can choose an appropriate and reliable form of dispute resolution. The Kuwaiti courts' respect for international arbitration agreements is encouraging. With suitable reform of the legislative framework it is hoped that arbitration, both international and domestic, may be embraced more widely in Kuwait.

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SENIOR ASSOCIATE

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1. Law No. 11 of 1995 Concerning Judicial Arbitration in Civil and Commercial Matters.
2. Law No. 38 of 1980 Promulgating the Civil and Commercial Procedures Law.

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"While historically third party funding has not been widely used in construction disputes, we predict that this is likely to change. "

THIRD PARTY FUNDING IN ASIA PACIFIC: AN UPDATE

One of the hottest topics at the moment is third party funding [TPF], with the demand for TPF growing regionally, and globally. While critics of TPF allege that it has been used to support impecunious parties, it is increasingly used for risk and asset management, and to add value to proceedings.

With Hong Kong becoming the latest country in the Asia-Pacific region to permit TPF, it is a timely occasion to take a closer look at the development of TPF in Hong Kong and its growing prominence in the wider region including Singapore, Australia and New Zealand.

What is TPF?

TPF is an arrangement where a person with no legal interest in the proceedings (other than under the funding agreement) funds the costs and expenses of the proceedings in exchange for an agreed return.

TPF is usually provided by specialist funders. However, the market has now expanded to include other financiers such as insurance companies, investment banks, hedge funds and law firms.

Why TPF?

There are many advantages to TPF. For one, it can provide access to justice for parties who would not have otherwise been able to resource proceedings. Further, it can offer a convenient financing structure so that capital is not tied up in proceedings, be used to manage risks associated with bringing or defending proceedings or to add value to proceedings by providing parties with access to otherwise cost prohibitive expertise or technologies in support of their case.

However, TPF is not without its drawbacks. For example, it may result in undisclosed conflicts of interest (e.g. where there is a pre-existing relationship between a funder, party and/or acting law firm), breaches of confidentiality and privilege, and a funder exerting improper influence over proceedings.

Barriers to TPF?

The most significant barrier to TPF in the common law world is the antique English doctrine of maintenance and champerty which prohibits a third party with no legitimate interest in a proceeding from supporting or maintaining the proceedings in exchange for a percentage of the proceeds. The application of this doctrine to the jurisdictions the subject of this article is discussed below.

Hong Kong

The Code of Practice for Third Party Funding of Arbitration and Mediation [Code] came into effect on 1 February 2019 setting out the practices and standards that funders are ordinarily expected to comply with in carrying on activities in connection with TPF of arbitration and mediation in Hong Kong including the scope of funding agreements, termination of funding agreements, capital adequacy, conflicts of interest, control of proceedings and liability for adverse costs.[1]

This development follows the 2017 amendment to the Arbitration Ordinance [Cap 609] which provided that TPF of arbitrations and related litigation and mediation proceedings are not prohibited by maintenance and champerty.[2] This amendment extends to arbitrations in Hong Kong and outside of Hong Kong for services provided in Hong Kong, and is not limited to specialist funders.[3]

1 There is no regulatory framework in Hong Kong. Under Section 98S of the Arbitration Ordinance (Cap 609) the failure to comply with the Code does not, in itself, render any person liable to any judicial or other proceedings, however, the Code is admissible in evidence in proceedings before the courts and tribunal and may be taken into account if it is relevant to a question being decided by the courts or tribunal.

2 The amendment (Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Ordinance) was passed by the Legislative Council on 14 June 2017. Arbitration Ordinance (Cap 609), Sections 98K, 98L.

3 Under Section 98J of the Arbitration Ordinance (Cap 609) a third party funder is defined as any *"person who is a party to a funding agreement…and who does not have an interest recognized by law in the arbitration other than under the funding agreement"*. This definition excludes law firms acting on a matter from providing any form of funding.

Funded parties are required to disclose that a funding agreement has been made, the name of the funder and the conclusion of the funding agreement.[4]

Outside of the above, TPF is generally prohibited in litigation except in: 'common interest' cases; where 'access to justice considerations' apply; and in limited miscellaneous circumstances including insolvency litigation.[5]

Singapore

In 2017 Singapore passed legislation abolishing maintenance and champerty in international arbitrations and related litigation and mediation proceedings.[6] Unlike Hong Kong, where TPF is guided by a Code and non-compliance does not carry any legal consequences, Singapore prescribes an extensive regulatory framework for TPF. For example, only specialist funders with a minimum 'paid-up' capital of SGD $5 million are eligible to provide TPF,[7] and solicitors acting for a party receiving funding must disclose the existence of a funding agreement as soon as practicable to the tribunal (or court) and other parties to the proceeding as well as the address and identity of the funder.[8] In addition, the Singapore Institute of Arbitrators has issued non-binding guidelines for funders and the Singapore International Arbitration Centre (SIAC) has issued a Practice Note on arbitrator conduct in SIAC cases involving TPF. More recently, Singapore passed the *Insolvency, Restructuring and Dissolution Act 2018* empowering liquidators to assign the proceeds of certain actions, for example, unfair preferences, undervalued transactions, extortionate credit transactions, fraudulent and wrongful trading, and delinquent officer's facilitating TPF, and to engage and increase their access to TPF.[9] Outside of the above, TPF is generally prohibited in litigation except in limited circumstances, for example, where funding is provided to investigate potential claims in connection with a major corporate collapse.[10]

Australia

TPF emerged in Australia in the 1990s, and it has since grown into one of the most active jurisdictions in the world. Unlike Hong Kong and Singapore, there is no limit on the availability of TPF. Nonetheless, TPF in Australia is not without complexity. Maintenance and champerty have not been abolished in a number of states and territories and therefore there is scope for funding agreements to be set aside in these jurisdictions. There is no specific regulatory framework. Instead, TPF is largely governed by the courts (and their respective rules) in each jurisdiction.

New Zealand

While maintenance and champerty have not been abolished, New Zealand courts have taken a pragmatic, 'cautiously permissive' approach to TPF providing parameters for the operation of TPF in New Zealand.

In particular, the courts have recognised a supervisory jurisdiction over funding agreements in representative actions.[11] Further, the courts have recognised an inherent power to prevent an abuse of process arising from funding agreements or claims under funding agreements which amount to impermissible assignment of a cause of action. There are also specific disclosure requirements for representative actions and non-representative actions. Impending reform is likely in New Zealand with the Law Commission announcing last year its intention to review class actions and TPF.[12]

Impact on the Construction Industry

While historically TPF has not been widely used in construction disputes, we predict that this is likely to change. With arbitration and mediation the primary means of dispute resolution under various standard form construction contracts, and TPF now available in leading arbitral seats of Hong Kong and Singapore, there is likely to be a greater use of TPF in the construction industry.

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4 Arbitration Ordinance (Cap 609), Sections 98, 98V. Under Section 98W of the Arbitration Ordinance (Cap 609) the failure to comply with compliance requirements does not, in itself, render any person liable to any judicial or other proceedings.

5 *Unruh v Seeberger* [2007] 10 HKCFAR 31.

6 Civil Law Act (Cap 43), Sections 5A and 5B. Related proceedings include proceedings to enforce an arbitral award.

7 Civil Law (Third-Party Funding) Regulations 2017, Regulation 4(1).

8 Singapore Legal Profession (Professional Conduct) Rules 2015, Section 49A.

9 Insolvency, Restructuring and Dissolution Act 2018 (No. 40 of 2018), Sections 99, 144 and 204. This Act is expected to come into force in the first half of 2019. See also *Re Vanguard Energy Pte Ltd* [2015] SGHC 156.

10 *Re Fan Kow Hin* [2018] SGHC 257.

11 Rule 4.24 of the High Court Rules (NZ).

12 https://www.lawcom.govt.nz/news/review-class-actions-and-litigation-funding.

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"Whether or not works are practically complete depends heavily on the facts"

WHEN ARE WORKS 'PRACTICALLY COMPLETE'?

In the recent case of *Mears Limited v Costplan Services (South East) Limited & Othrs*, the English courts considered the meaning of the phrase "practical completion".

The nature of the dispute

Mears Ltd (the tenant) entered into an agreement for lease [AfL] with a developer of two blocks of student accommodation. The AfL required the developer to procure construction of the blocks and, following practical completion, the tenant would enter into a lease for the accommodation. As the blocks neared completion, a dispute arose about whether they had been constructed in accordance with the AfL (a number of rooms had been built 3% smaller than set out in the planning permission), with the tenant alleging several breaches and obtaining an injunction preventing the issue of the practical completion certificate under the building contract.

The court's decision

The court granted a declaration that the blocks were constructed in breach of requirements in the AfL, but refused to accept that these breaches meant that practical completion could not be validly certified. The judgment includes some interesting observations about the meaning of the phrase "practical completion" and the circumstances in which it may, and may not, be certified.

The meaning of practical completion

In the contract in question, the term 'practical completion' was not defined and the court adopted a definition set out in *Keating on Construction Contract (9th edition)* that:

- Works can be practically complete notwithstanding that there are latent defects;
- A Practical Completion Certificate may not be given if there are patent defects;
- Practical Completion means the completion of all the construction work that has to be done; and
- The certifier is given a discretion... to certify Practical Completion where there are very minor items of work left incomplete on "de minimis" principles.

The court considered that for works to be 'practically complete', they do not need to conform with the contractual requirements in every way. Provided that any non-conformity is 'insignificant', the certifier must exercise its professional judgment in deciding whether or not to certify practical completion. The intent and purpose of a building is a key consideration.

When a building is intended to house people, whether or not it is fit for occupation is a key question and the answer will depend on the facts. But, the court also acknowledged that even where a building that was intended to house people was fit for occupation, it might still not be practically complete.

The breach in this case was not capable of being remedied without starting over and the Court considered how to deal with breach of a building contract that is incapable of being remedied (without starting again). To certify practical completion is a let off for the contractor in default. But, can an irremediable breach be adequately the compensated by the contractor paying damages to the employer? In the court's view, whilst an irremediable breach can prevent practical completion being certified, it will not always do so; it will depend on the facts.

Conclusion

Whether or not works are practically complete depends heavily on the facts, including the purpose of the works and the nature of any breach(es) by the contractor. It is common practice to specify work that must be completed for the purposes of practical completion. However, difficulties can arise if the parties try to create an exhaustive list of circumstances when 'practical completion' will or will not be certified.

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LIST OF UPCOMING EVENTS – 2019

Construction Quarterly Seminar
London
1 March 2019
Presenting: Max Wieliczko, Huw Wilkins, Chris Philpot

ADR and Arbitration in the Construction Industry Seminar
Bali International Arbitration and Mediation Centre
Jakarta
14 March 2019
Presenting: Ben Bury

HFW – Driver Trett Construction Seminar
Kuwait
19 March 2019
Presenting: Michael Sergeant, James Plant

Construction Insurance Seminar
Seoul
20 March 2019
Presenting: Nick Longley, Richard Jowett

5th Annual 10 CPD Point Conference
Sydney
20 March 2019
Presenting: Ian Gordon

Construction Week Awards
Oman
25 March 2019
Attending: James Harbridge, Beau McLaren

Adjudication Update Breakfast Seminar
Melbourne
26 March 2019
Presenting: Alex McKellar, Alastair Oxbrough

11th IBA Annual Real Estate Investments Conference
Dubai
27 – 29 March 2019
Presenting: Carolyn Chudleigh, Stephanie Lambert, Richard Abbott, Sydene Helwick

Construction Quarterly Seminar
Sydney
4 April 2019
Presenting: Alex McKellar, Sophy Woodward, Jarrod Gutsa

Women in Business: Infrastructure Seminar
Hong Kong
11 April 2019
Presenting: Ben Bury

CIArb Asia-Pacific Regional Conference 2019
Singapore
23 April 2019
Presenting: Nick Longley

Construction Quarterly Seminar
London
14 – 15 May 2019
Presenting: Michael Sergeant, Richard Booth

HFW Offshore Day
London
22 May 2019
Presenting: Richard Booth

8th Annual Advanced Submarine Power Cable and Interconnection Forum
Berlin
12 – 13 June 2019
Presenting: Richard Booth

19th Construction Law Summer School
Cambridge
2 – 6 September 2019
Presenting: Michael Sergeant, Ben Mellors

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