Construction

March
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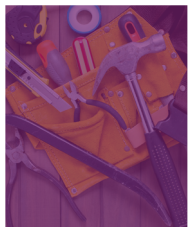
CONSTRUCTION BULLETIN





Welcome to the March edition of our Construction Bulletin

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

- **New FIDIC forms of contract:** Michael Sergeant comments on the new FIDIC forms of contract, scheduled to be issued this year, and in particular the revised variation provisions.
- **Peripheral disputes: pressure and potential:** David Ulbrick considers how peripheral disputes can create opportunities for parties to a dispute to discuss settlement opportunities at an early stage.
- **Contractor victorious in tunnel collapse claim:** Katherine Doran considers Hochtief's recent victory in court proceedings brought by SSE and gives an insight into some interesting legal issues arising from the NEC form of contract used on that project.
- **Welcome to new construction partners:** Max Wieliczko introduces HFW's two new construction partners: Ben Mellors and Beau McLaren.

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

Should you require any further information or assistance on any of the issues dealt with here, please do not hesitate to contact any of the contributors to this bulletin or your usual contact at HFW.

Michael Sergeant, Partner, michael.sergeant@hfw.com

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New FIDIC forms of contract

The current standard form FIDIC contracts were issued in 1999. FIDIC aims to publish revised versions of its contracts this year and has started with the Yellow Book.

HFW has sponsored the FIDIC conferences in London and the Middle East for the last three years. This is an interesting time for the FIDIC forms of contract. These contracts are very widely used internationally, in particular in the Middle East, Africa and South East Asia. They are also becoming increasingly commonly used on UK projects, with off-shore wind farm projects commonly let under amended Yellow Book contracts.

At the recent FIDIC conferences, in London in December 2016 and Abu Dhabi in February 2017, a pre-release version of the new 2017 Yellow Book was made available for delegates. FIDIC has decided to start with a revised version of the Yellow Book, which has been circulated as a means of attracting industry comment, before finalisation later this year. The plan is to also publish revised versions of the Red and Silver Books later this year.

The new contract has provoked considerable discussion and Max Wieliczko and I gave a talk at the most recent conference on issues arising in relation to the variations clause under the new Yellow Book.

The new contract introduces more structured, but complex, processes. These aim to get disputes resolved as the project goes along. As with the NEC forms of contract, these systems inevitably require the parties to undertake more contract

The new contract introduces more structured, but complex, processes.

MICHAEL SERGEANT, PARTNER

administration during the project. The potential downside is that the contract mechanisms may be too complex for certain projects with the risk that they are not followed, potentially leading to greater uncertainty. The new approach to variations is a good example.

Under the 1999 Yellow Book, a variation instruction had to be in writing (for example email) but other than that did not have to be in any specified format or use any special wording. The new contract completely changes that simplified approach. The instruction must identify itself as a "Notice" and state that the work requested is a "Variation". If it does not, then the contractor must flag this up and give notice to the Engineer. If the contractor undertakes the work without getting such a formal notification that it is a "Variation" then it will not be entitled to additional payment.

For all instructed variations, the contractor must give the Engineer full details of its proposed price and the impact on the project programme, with the aim of these being agreed contemporaneously.

If the parties cannot agree whether certain work is a variation, then there is a danger that there will be a stand-off on site. In other words, the Engineer will not issue an instruction in the specified format and the contractor will not do the work without it.

The new contract has procedures to resolve such disagreements. The contractor has to give notification of a claim which the Engineer is under an obligation to resolve within 42 days. If the Engineer confirms his original decision, and says that the work is not a variation, then the contractor must refer the issue to the Dispute Adjudication Board (DAB) within a month or lose the right to appeal.

The DAB has 84 days to make a decision. If it decides that the item of work is not a variation then the contractor will again have to serve a notice of dissatisfaction within a month and have the issue resolved via arbitration.

There is no question therefore that the new contract sets down a much more structured approach. Taking the process for instruction of variations as an example, it can be seen that the new contract brings matters in disagreement to a head, rather than letting them fester.

Any disagreement as to whether an instructed item of work is a variation cannot be left until the final account stage as is currently the case. The parties must address the issue straight away. However, it is a system which is more likely to lead to stand-offs on site and multiple arbitrations on contested issues.

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Peripheral disputes: pressure and potential

Peripheral disputes, such as jurisdictional challenges and security for costs applications, often arise in the course of disputes. We consider the extent to which these peripheral disputes can assist the parties in discussing settlement options.

What are peripheral disputes?

No project manager sets out to have a dispute with its contractual counterparty about issues such as whether they should be allowed to continue a court proceeding or go before an arbitrator to resolve the dispute; whether a document they wrote in the middle of the job is subject to legal professional privilege; or whether the adjudicator who just determined a dispute in their favour committed jurisdictional error in doing so because he forgot to attach a spreadsheet to an email in the middle of the night.

Why do peripheral disputes arise?

These sorts of disputes occur in most jurisdictions in the common law world. The reason is deceptively simple: running a complex construction case where there are multiple claims for variations, delays and disruptions is hard work. It takes a large multi-disciplinary team working together over many months to put a case together. Then another equally talented multi-disciplinary team works together for many months to pull it apart. Finally, a judge or arbitral tribunal is then asked to decide who was right - a process which itself can take many months, if not years. In some jurisdictions this can be further lengthened and complicated by having many parties involved in the litigation.

What opportunities arise from peripheral disputes?

These seemingly peripheral disputes about matters such as privilege, security for costs, or disputes about the proper forum for resolving a dispute can offer a way of getting to a resolution sooner than going through the pain and distraction of a full trial. This is because, while they are legitimate steps for litigants to take (indeed they are usually aimed at ensuring the dispute process is fair to all concerned) they have the collateral effect of creating pressure and additional negotiation points.

The pressure comes from the need to address and engage in the peripheral dispute - once it starts it must be dealt with. For example, in a security for costs application, a respondent who doesn't wish to put up the requested security must come up with an argument why the application is not warranted. To do that it will undoubtedly need to review the relevant legal position and file evidence about its solvency. However, it may also need to engage a costs expert to challenge the claimant's estimate of its costs or brief an advocate to appear in any hearing of the issue. All of these steps have the inevitable effect of distracting the litigant from the main dispute.

Furthermore, additional negotiation points arise because each peripheral dispute is its own mini-trial and so (at least in common law jurisdictions) adheres to the usual pattern of pleadings, evidence, submissions, a hearing and then a decision. The usual negotiation points for any dispute apply equally to these peripheral disputes: at the close of pleadings and the close of evidence/submissions.

These seemingly peripheral disputes ... have the collateral effect of creating pressure and creating additional negotiation points

DAVID ULBRICK, SPECIAL COUNSEL

Without the peripheral dispute it may be many months between commencing the proceedings and the first of these "natural" negotiation points. However, the existence of a peripheral dispute can create an opportunity for the parties to negotiate much earlier and, importantly, there is no rule which says that the negotiation point created by the existence of the peripheral dispute must be confined to that issue. So there is an opportunity for the parties to settle everything, perhaps earlier than would otherwise be the case and with the additional knowledge about how each party approaches the formal dispute resolution process. That can only be good.

For more information please contact David Ulbrick, Special Counsel, on +61 (0)8 9422 4701, or david.ulbrick@hfw.com, or your usual contact at HFW.

hfw Contractor victorious in tunnel collapse claim

HFW successfully acted on behalf of Hochtief in a dispute over a major tunnel collapse at the Glendoe Hydro Electric Plant in the Highlands of Scotland. Hochtief defeated a £200 million claim brought by energy giant SSE by establishing that it was not liable for the collapse.

One very practical issue arising was the possible adverse impact that the NEC standard wording had on the administration of the contract, and the approach the contractor was forced to adopt in its defence at the trial.

KATHERINE DORAN, ASSOCIATE

In December 2016, the Court of Session in Scotland issued its decision in a case concerning liability for the collapse of a section of the headrace tunnel at the Glendoe Hydro Electric Plant. Hochtief completed the project in December 2008, but power generation came to a halt just eight months later, in August 2009.

The water-bearing headrace tunnel was constructed through hard rock using a Tunnel Boring Machine and was designed to be substantially unlined, with only localised support. When the tunnel was dewatered it was found that there had been a major rock fall, and it was eventually ascertained that a 71 metre stretch of tunnel was completely blocked with debris, from the invert to tunnel crown. A further 600 metres of debris only partially filling the tunnel cross section extended in a pile downstream of the fully blocked zone. The length of the tunnel crown which had actually collapsed was never finally established, and was a major area of dispute between the parties. SSE originally asserted it was 270 metres long, later reducing its claimed collapse length to 71 metres. Hochtief meanwhile contended that the actual collapse was in fact a maximum of only 15 metres in length.

SSE also claimed that there were 114 secondary features outside of the collapse zone where the support of the tunnels was supposedly inadequate, and which also constituted defects in Hochtief's design.

SSE's position was that the collapse and secondary features were down to inadequate rock support caused by Hochtief's allegedly incorrect rock classification. This informed SSE's decision to substantially line the entire headrace tunnel as part of the remedial scheme. Hochtief argued that the secondary features identified by SSE either required no additional support (because they were entirely typical features of an unlined tunnel of this nature) or were normal maintenance features to be expected on a first dewatering of any comparable unlined tunnel and which could have been addressed through the application of localised support, such as additional rock bolts or shotcrete.

History of the Dispute

A dispute arose between SSE and Hochtief concerning liability for the collapse, and who should bear the cost of the remedial works as they proceeded. SSE asserted that the collapse and secondary features were due to defective design because the rock support which Hochtief had installed in the tunnels was inadequate.

An important facet of the dispute was SSE's presumption from the outset that Hochtief was liable until such point as Hochtief could establish otherwise. This was in part based on SSE's interpretation of the contract, which reversed the burden of proof in relation to defects of design. The clause in question of the NEC contract provided that *"the Contractor is not liable for Defects in the works due to his design so far as he proves that he used reasonable skill and care to ensure that his design complied with the Works Information"*[1].

In the more usual course of things under other contracts, it would be for a party alleging defects (usually the employer) to establish that there is a design error, and that the contractor failed to exercise reasonable skill and care. The NEC form however, places the onus on the contractor to prove that he has not been negligent. This

1 Note that Option M of NEC2 is in the same terms as Optional Clause X15.1 of NEC3



will often require contractors to prove the entire construction process was reasonable and appropriate.

Following the collapse, SSE sought to influence the extent and nature of the remedial works (despite Hochtief being the design and build contractor and liable for the performance of the design). SSE also insisted on Hochtief bearing half the cost of all the remedial works, even though SSE acknowledged that liability had not been established. As a result, the parties failed to agree a basis for Hochtief to undertake the remedial works, and SSE went on to appoint a replacement contractor to execute the recovery works.

The recovery works commenced in March 2010 and primarily consisted of the construction of a massive 605 metre long bypass tunnel around the fully blocked zone but also a major part of the downstream debris pile; the construction of an approximately 500 metre long downstream access tunnel; and the full circumferential lining of approximately 70% of the headrace tunnel.

After SSE made a call on the on demand performance bond, Hochtief commenced an adjudication in 2011, seeking a decision that it was not liable for the collapse. Following a five month process the adjudicator, Mr Robert Gaitskell QC, found that the collapse was an employer's risk, and Hochtief therefore had no liability to SSE.

The Court Case

In December 2012, SSE commenced proceedings in the Scottish Court of Session, seeking to overturn the adjudicator's decision, and claiming £200 million from Hochtief (including £130 million for the cost of repairs, and £65 million for loss of profit[2]).

The case was one of the longest and most technically complex to come to trial in Scotland in recent years and was held between October 2015 and April 2016. The court sat for 87 days and over 73,000 documents in evidence were lodged in the electronic bundle, including 40 expert reports and 103 witness statements.

19 experts gave evidence and there was innovative use of an animation and 3D modelling during the trial to help explain the complex geotechnical concepts which went to the heart of liability. This was also the first occasion in Scotland where expert evidence was taken concurrently, in a procedure colloquially known as "hot-tubbing"[3].

The Decision

In finding in favour of Hochtief, the judge considered the contractual provisions whereby the contractor is not liable for defects in his design so far as he proves that he used reasonable skill and care to ensure that it complied with the works information. Lord Woolman held that this provision *"placed an important brake on liability"* and held that the effect of the contract was that *"Hochtief did not guarantee the works"*.

The judge found that Hochtief had discharged the burden of proof. In order to get to this position, however, Hochtief had been faced with the considerable challenge of proving a negative: that it had not been negligent. This entailed demonstrating that everything it did – from early design decisions, to the tunnelling and mapping processes, the selection and installation of support, and the on-site processes for undertaking snagging and take over – were all done competently and were not negligent. This contributed, in no small measure, to the length and complexity of the trial.

Hochtief was held not to be liable for the collapse which the judge again confirmed was an employer's risk event. The judge also concluded that none of the other 114 features identified in the tunnel by SSE were defects. SSE was therefore unable to recover any of the reinstatement costs incurred following the collapse.

Comment

One very practical issue arising was the possible adverse impact that the NEC standard wording had on the administration of the contract, and the approach Hochtief was forced to adopt in its defence at the trial. Because the contract reversed the burden of proof, SSE insisted on Hochtief bearing half of all the cost of reinstatement works as a pre-condition to carrying out the remedial works. This contributed to SSE's decision to appoint an alternative contractor. Furthermore NEC's reversal of the burden of proof greatly contributed to the length and complexity of the trial.

Hochtief contended that under the NEC forms of contract all damage to the works after Take Over is presumed to be an employer's risk event until determined otherwise. Unfortunately SSE did not administer the contract to reflect this and appeared to have misunderstood as to what the contract required.

For more information please contact Katherine Doran, Associate, on +44 (0)20 7264 8110, or katherine.doran@hfw.com, or your usual contact at HFW.

2 SSE was later forced to accept that the contract limited any claim for loss of availability of the Plant at £1 million

3 Hot-tubbing was discussed in our September bulletin: http://www.hfw.com/Construction-Bulletin-September-2016

Welcome to new construction partners

I am delighted to be able to announce that this month two new Partners are joining HFW's international construction team.

Ben Mellors joins us in our London office, and Beau McLaren will be based in Dubai, where he has worked for eight years.

Both individuals are very experienced construction lawyers specialising in all aspects of construction law, both in relation to project set up and support, and also complex dispute avoidance and resolution.

A major part of the work undertaken by Ben and Beau is in the Middle East, and in common with the rest of the HFW construction team they are also used to providing hands on project support in all its forms in a variety of other jurisdictions, including Europe, Africa and Asia.

Ben Mellors

Ben has a proven track record of working with a variety of construction participants internationally, including project sponsors, funders, consultants and of working around the world for a number of international contractors and developers, including Turkish, Korean, African, Middle Eastern and Chinese.

Ben specialises in advising clients on all sides of the engineering and construction industry on both the contentious and non-contentious aspects of international on and off-shore construction and engineering projects. He has a particular focus on the Middle East and Africa, with expertise in major transport, infrastructure, power, and oil and gas projects, and the FIDIC forms of contract, which are the most widely used forms of contract in international construction.

Ben was co-author of the well known industry text book "FIDIC Contracts: Law and Practice" (published by Informa in 2009), which is from the same authoritative construction practice series stable as "Construction Contract Variations" a text book co-authored by Michael Sergeant and me in 2014.

In addition to FIDIC, Ben has extensive experience of a broad range of other standard form contracts, including ICC, ENAA, EDF, JCT, NEC, ACE, IChemE, and GC/Works, as well as project specific EPC contracts and other bespoke agreements and forms of Public Private Partnership (PPP) projects.

Ben has a particular interest and expertise in avoiding and solving complex, high-value problems and disputes in the international construction industry. He has significant experience acting for all sides of the engineering and construction industry in ICC, UNCITRAL, DIAC, and 'ad hoc' arbitrations, as well as litigation in the English Technology and Construction Court, adjudication, dispute boards, negotiation, mediation, and further forms of ADR.

He is a Solicitor-Advocate with Full Higher Rights of Audience in the English Courts, a registered Legal Consultant in Dubai and a qualified barrister. Before turning to the law, he practiced as a civil engineer at Atkins, a leading international consulting engineering company with offices around the world, including in the UK and the Middle East.

Beau McLaren

Beau McLaren joins us in our Dubai office and has worked in the Middle East for the last 8 years, having been a construction lawyer since 2005. He studied at University College London, and initially qualified as a specialist non-contentious lawyer in London where he gained considerable experience of major infrastructure projects in the United Kingdom and abroad, including PPP Schemes.

...we are particularly pleased to have been able to strengthen our firm, by having Ben Mellors and Beau McLaren join us

MAX WIELICZKO, PARTNER

Beau acts for the complete range of construction industry participants including banks, developers, domestically based and international contractors and he has advised throughout the Middle East, including the UAE, the Kingdom of Saudi Arabia, Qatar, Oman and Kuwait. He also has extensive experience acting outside of the Middle East including Africa and Europe.

As well as considerable experience of dispute resolution in the DIFC and onshore court proceedings, Beau has extensive experience of both the prosecution and defence of domestic and international arbitration under various institutional and 'ad hoc' procedural rules.

As head of HFW's international construction team, I can say that we are particularly pleased to have been able to strengthen our firm, by having Ben Mellors and Beau McLaren join us, and our clients will benefit accordingly.

For more information please contact Max Wieliczko, Partner, on +44 (0)20 7264 8036, or max.wieliczko@hfw.com, or your usual contact at HFW.



Conferences and events

Construction Quarterly Seminar
The revised SCL Protocol and a review of the challenges in relation to concurrent delay
Sydney, Australia
7 March 2017
Presenting: Max Wieliczko and Nick Watts

HFW Quarterly Seminar
The revised SCL Protocol and a review of the challenges in relation to concurrent delay
Perth, Australia
10 March 2017
Presenting: Max Wieliczko and Matthew Blycha

Benchmark developments in Expert evidence
Singapore
14 March 2017
Presenting: Max Wieliczko, Chanaka Kumarasinghe and William Duthie

Construction Quarterly Seminar
NEC and Glendoe case Study
Hong Kong
15 March 2017
Presenting: Max Wieliczko and Martin Downey

National Association of Women in Construction
Running interference and how to stay the course
Perth, Australia
22 March 2017
Presenting: Matthew Blycha and David Ulbrick

Property Council of Australia
Property Development & Construction Seminar – Advanced course
Sydney, Australia
27 March 2017
Presenting: Carolyn Chudleigh

Quarterly Breakfast Seminar
Middle East Construction Contracts
Dubai
26 April 2017
Presenting: Beau McLaren, Ben Mellors and Michael Sergeant

HFW Industry Seminar Series 2017
Construction of Renewable Energy Projects: Issues and Solutions
Perth, Australia
3 May 2017
Presenting: Matthew Blycha and Simon Adams

Agribusiness Law Conference
Reliance on Infrastructure and Construction - Continuing Legal Education Conference
Melbourne, Australia
3 - 4 May 2017
Presenting: Carolyn Chudleigh

Hill International Masterclass
Offshore Construction contracts
Singapore
4 May 2017
Presenting: Matthew Blycha

University of Melbourne
Managing Risk in Construction
Melbourne, Australia
8 - 12 May 2017
Presenting: David Ulbrick

Kluwer Middle East Arbitration Conference
Qatar
17 May 2017
Presenting/Attending: Damian Honey, Michael Sergeant and Max Wieliczko

HFW Quarterly Construction Seminar
London
23 - 24 May 2017
Presenting: Max Wieliczko and Ben Mellors

HFW Industry Seminar Series 2017
Lessons learned from urban rail developments
Perth, Australia
21 June 2017
Presenting: Matthew Blycha and David Hardiman (Driver Trett)

MBL Construction Law Conference
Problem clauses in construction contracts
London
13 July 2017
Presenting: Michael Sergeant

HFW Industry Seminar Series 2017
Innovation and the use of technology in Construction in Australia
Perth, Australia
3 August 2017
Presenting: David Ulbrick

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