Mechanisms to control poor contractual performance

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Gatton

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Goals for your project

- Time
- Cost
- Quality
What are the risks which are ‘outside’ of control?

- step back and consider the risks

- expected weather
- unexpected weather
- ground conditions
- international trade embargo
- government approvals
- new technology
- fire
- terrorism
- change in law
- short supply of goods
What are risks typically ‘within’ contractor’s control?

- Under Bidding / Programming
- Warranty / Defects
- Insolvency
- Legislative Breaches (WHS / Enviro, etc.)
- Intellectual Property
- Disputes / Internal Resources
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Risk allocation – who should bear the risk?

- Early identification of risk
- Who can control/manage the risk
- Who can take action to address the risk for least $
- Where should the economic incentive be to manage risk (negative / positive)
- What is most efficient (including dealing with innovation)
Liquidated damages (LDs) - parties agree on amount payable as compensation for a particular breach of contract / performance issue.

Examples of breaches where LDs are commonly used:

- failure to complete on time / in accordance with an agreed schedule
- failure to meet a performance criteria
- availability of key personnel
- KPIs (service level, safety, environment, etc.)

No need to prove actual loss – entitled to recover the agreed amount of LDs.

In formulating an LD – must be a genuine pre-estimate of loss.
Economic incentives (positive)

- open book / direct costs (fluctuating margin)
- milestone payments (tied to specific performance)
- bonus (time / performance / KPIs, etc.)
- value management (share of savings)
Other considerations

- what about flexibility
  - termination for convenience
  - variations
  - notice to proceed
  - acceleration

- overall alignment - responsibility ‘single point’ (?)
  - novation
  - residual

- secondary risk allocations
  - take out insurance
  - provision of security
    - bank guarantee
    - deed of guarantee and indemnity from parent company or director
Common law (limited excuse rights)

- **Ooh! Media Roadside Pty Ltd (formerly Power Panels Pty Ltd) v Diamond Wheels Pty Ltd [2011] VSCA 116**

- A relatively simple set of facts was considered:
  - There was a licence granted to use a site for a ‘permitted use’ of outdoor advertising.
  - A large sign board was erected on the roof of a building in a city.
  - The line of sight from a major road to the sign was obscured by a new building on land which was previously vacant.

- The claim was that the contract had been frustrated.
Need for a contractual clause

a case considering a force majeure clause

- Holcim (Singapore) Pte Ltd v Precise Development Pte Ltd & Anor 1 [2011] SGCA 1 the Court of Appeal in Singapore

case was considering the Indonesian sand ban, which meant Holcim could not supply sand under a contract

in connection with the ‘force majeure provision’, the relevant excerpts of the clause read:

‘The Supplier shall be under no obligation to supply concrete if the said supply has been disrupted by virtue of ... shortage of material ... arising through circumstances beyond the control of the Supplier.’

the Court determined that Holcim was relieved in the circumstances
Some excuse clauses (AS2124)

- Clause 8.1 – Discrepancy in the Contract Documents
- Clause 12 – Latent Conditions
- Clause 14 – Change in Law
- Clause 16.3 – Excepted Risks (negligence of Principal, war, invasion, insurrection, usurped power, radiation, use or occupation by the Principal, defects in the design)
- Clause 17 – Claims in respect of the right of the Principal to construct the work on the Site
- Clause 27 – Finding of minerals, fossils and relics
- Clause 28 – Errors in setting out the works
- Clause 33 – Rate of progress – compliance with directions of the Superintendent
- Clause 35 – Extensions of time (industrial relations, inclement weather, Principal caused, changes in law, directions by municipal or statutory authorities)
- Clause 40 – Variations (‘direction’ definition – change to character of the work)
- Clause 45 – Termination by Frustration
- Clause 46 – Notice of Intention to Claim (‘direction’ definition)
It was announced that Council will have a wonderful new water park and kiosk built within 9 months in time for the start of summer 2020 (with a budget of $3 million for construction).

Council commissions a geotechnical report of the area to get things moving on the project.

Council’s team also engages an architect to draw up the plans for the design using the architect’s standard terms (and the architect subcontracts work to engineers).

Following the design completion, Council goes out to market with an unamended AS2124 to appoint a contractor to demolish the library building and construct the water park.

Council appoints New Kids Pty Ltd after a tender process (who were just under budget with an offer $2.9 million).

New Kids have a construction program showing 6 months to complete (which would allow delivery of the project just before summer) and liquidated damages are stated to be $1,000 per day.
Poor contractual performance (example 1)

New Kids work does not appear to be progressing on time. New Kids verbally acknowledges they have some resourcing issues but nevertheless states it will get the work done on time. The Superintendent requests a program for the work. A rudimentary program is provided showing work at a very high level only. The Superintendent believes the program is deficient to monitor the work and progress in any meaningful manner.

The Superintendent requests an updated and more detailed program and a progress report on a weekly basis along with a weekly site meeting. At the weekly site meeting the Superintendent makes comments on the documents and explains what work should be done by New Kids in the upcoming week.

New Kids claims the process is a variation and that New Kids is entitled to recover for the additional administration being imposed. New Kids also fails to comply with a number of the Superintendent’s requests and tells the Superintendent it cannot reasonably do so due to some of the resourcing constraints it faces.

When New Kids does comply with an instruction of the Superintendent, it also typically makes a claim that it is entitled to additional costs (based on the Superintendent requesting an acceleration of work).

On one occasion New Kids actually claims that the re-sequencing of the methodology requested by the Superintendent has caused them delay and that entitles them to a one month extension of time and delay costs (which it claims from Council at a rate of $3,500 per day).
Poor contractual performance (example 2)

New Kids has their licence suspended by the QBCC. Most of New Kids’ workers are taken off site and New Kids tells Council it might take them a month to appeal the process with the QBCC to regain their licence.

There is minimal work left to complete at the water park however Council does not want to award practical completion yet with the job not done (it is also missing the necessary building certifications, as-built drawings and O&M manuals).

Council waits for a month and New Kids has still not resolved the issue with the QBCC licence. Council is subsequently advised that New Kids has entered into administration. The work is still not complete and a grand opening day Council had planned is less than a week away.
The park has opened and for the first few months it appears to be a great success. However it is not long before concrete and walls around the pools are found to be cracking due to structural / subsidence issues.

New Kids have recovered from their administration but are refusing to rectify any of the issues as defects as they claim the error is in design. The architect has stated they are not to blame but they cannot verify the engineer’s work to the extent the issues are with respect to the structure. The architect also notes that the issues could have arisen if there were errors in the geotechnical report which Council has separately commissioned.

Council officers have attempted to contact the engineer but the engineer has advised Council that they have no contract with Council so they are not in a position to respond to Council.

Due to safety concerns the water park is shut down by Council indefinitely.
Approach to avoiding poor contractual performance

- early project workshops (variety of people involved)
- understanding of key issues / risks
- due diligence (financial & technical)
- whole of project alignment
- processes established
- implementation (contractual documentation)
- monitoring and reporting
- reacting / utilising flexibility provisions
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