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Legal Update

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New year – time for change

Welcome to the first Construction & Engineering Legal Update of 2008 – with a difference and an international theme.

We focus first on international contracting, starting with Jonathan Hosie's analysis of why and how the FIDIC Silver Book need skilful tailoring to suit your requirements. We then dip into the pre-press edition of the FIDIC Gold Book and the new IChemE International Forms and look at a case about an equitable lien and an oil rig - with possibilities.

And then there's a round-up of news on the domestic front - adjudication post Melville Dundas, corporate manslaughter and the axing of PGS for starters, plus an update on some significant recent events at Mayer Brown.

We hope you find the contents of interest and may we wish you all, at this first opportunity, a very good 2008.

On the international front...

Customising the Silver Book

It would be remarkable if one size of contract were to fit all types of project. Take, for example, the FIDIC Conditions of Contract for EPC Turnkey Projects (the Silver Book).

FIDIC Silver projects transfer to the contractor responsibility to engineer, procure and construct the required facility. The finished facility should meet the Employer's Requirements and be capable of delivering its required output or performance, once the project is handed over and the Employer turns the key.

The challenge for those who adopt FIDIC Silver for EPC Turnkey projects is to assess the "*pinch points*", where the particular features of the project do not fit neatly within the EPC Turnkey model.

Under an EPC contract in the power sector, for instance, the Contractor can be expected to assume full performance risk for the achievement of power output, efficiency/heat consumption etc, because it can manage its own technology. In contrast, under an EPC in a petrochemical project, the outputs will often depend on the performance of proprietary technologies owned and supplied into the project by third parties and so the EPC Contractor is less able to assume responsibility for the achievement of the required outputs. This creates a pinch point as this segregation of responsibility is at variance with the EPC model, where the fundamental obligation on the EPC Turnkey Contractor is to produce all engineering, procurement, construction, commissioning and testing necessary to complete the project, so that it achieves its required performance outputs by a fixed date and at a fixed (lump sum) price. Some types of project provide a better fit for the EPC Turnkey model than others.

Further pinch points arise in those areas of commercial risk transfer where FIDIC Silver may be seen as less than ideal, by Employer or Contractor.

Having made a case for adapting FIDIC Silver to cater for pinch points (whether in the model or at the specific risk allocation level), it is instructive to look at what FIDIC Silver says on an issue, how, in practice, the parties seek to adapt the FIDIC Silver Book and why. This analysis uses two areas of FIDIC Silver to illustrate the process:

- limitations of liability;
- time periods for claims.

Limitations of liability - amendments under FIDIC Silver

Let us start with the proposition that Clause 17.6 of FIDIC Silver is far too broad an exclusion of liability. What does FIDIC Silver say and what might it say, if the parties accept this proposition?

The first part of Clause 17.6 (subject to limited exceptions in respect of payment on termination and indemnities) excludes certain types of loss:

"*Neither Party shall be liable to the other Party for loss of use of any Works, loss of profit, loss of any contract or for any indirect or consequential loss or damage which may be suffered by the other Party in connection with the Contract...*"

However, the key point centres on what that type of loss is.

English common law: direct and indirect loss

Assuming the contract is governed by English law, ***Hadley v Baxendale*** is the starting point for determining what loss may be recoverable for breach of contract. The first limb of the decision permits recovery of loss arising as a direct result of the breach. The second limb covers loss which both parties are presumed, at the time of making their contract, to have anticipated (in the light of their special knowledge) to be a reasonably foreseeable consequence of the breach. These two limbs are sometimes referred to respectively as "*direct*" and "*indirect*" losses.

Against this analysis, Clause 17.6 of FIDIC Silver excludes indirect but not direct losses. In addition, Clause 17.6 identifies specific types of loss, for which liability is excluded - "... *loss of use of Works, loss of profit, loss of any contract ...*".

Contracts in the process engineering sector frequently also identify other specific types of loss, including loss of catalysts and raw materials. However, it is not possible, at contract stage, to anticipate every type of loss which may occur or the way in which every claim may be framed, particularly where the contractual setting is complicated. Parties may therefore use a sweep up phrase such as that in Clause 17.6, to the effect that liability is excluded "*for any indirect or consequential loss or damage*". That may, however, raise issues of interpretation where a particular head of loss in question falls outside the other categories specifically excluded.

Deepak Fertilisers and Petro Chemical Corporation v Davy McKee (London) Limited & ICI Chemicals & Polymers Limited illustrates the point. Davy's contract with the Claimant involved the sale by Davy of a process licence, design and know-how in relation to the proposed design, construction, operation and maintenance of a methanol plant in India. After completion the plant exploded and had to be rebuilt.

The claim against Davy comprised a number of different heads of claim. These included the fixed costs and overheads referable solely to the methanol plant during the period from the time of the explosion until the resumption of commercial production as well as loss arising from the fact the re-constructed plant used more catalyst per charge than the original. In defence, Davy relied upon the following exclusion clause:

"*... and in no event shall Davy by reason of its performance or obligation under this contract be liable ... for loss [of] anticipated profits, catalyst, of all material and products all for indirect or consequential damages.*"

The English Court of Appeal decided that the fixed costs and overheads claimed were not indirect or consequential; they were the direct and natural result of the destruction of the plant and had not been excluded elsewhere in the clause. Similarly, the claim for the extra costs of the catalyst was not a claim for indirect or consequential damages. This was because the Court found that such costs were like any other costs which were necessarily incurred to ensure and enable the plant safely to produce the methanol in the expected quantities. Liability for additional catalyst costs as well as fixed costs and overhead losses was therefore not excluded by the contract wording.

In complicated contracts (which FIDIC Silver projects often are), it is common for the party engaged on a turnkey basis to know the special circumstances which would allow losses to be recoverable under the second limb of ***Hadley v Baxendale***. If that special knowledge exists, the court normally does not have to draw a distinction between the two limbs. The distinction becomes vital, however, if the court has to decide whether

the loss is consequential (i.e. indirect) because the contract excludes or limits liability for consequential damages and claims made are not obviously caught by the exclusion.

Ultimately, the best course is to identify expressly the types of loss (direct or indirect) that the parties agree should be excluded.

Cap on liability

Clause 17.6 also includes a cap on liability, normally expressed as a percentage of the Contract Price or, in default, as the Contract Price. The cost of delayed or deficient performance on a revenue producing project can be very great and most contractors will prudently want some cap on liability.

Compliance with applicable laws under Clause 1.13 of FIDIC Silver is a fundamental obligation of the Contractor which is often excluded from the cap.

Carve-outs from the cap

The rider at the end of Clause 17.6 carves out, from the exclusion clause, "*…fraud, deliberate default or reckless misconduct…*" In practice, it is common to see amendments proposed that also exclude claims arising from "*… gross negligence, wilful misconduct and abandonment of the Works*."

In addition, many FIDIC Silver provisions oblige the Contractor to complete the Works and to proceed at its cost in the case of re-work. Parties sometimes list all these other express remedies (for example Clauses 5.8 (Design Error), 7.4 (Testing) and 9.4 (Failure to Pass Tests on Completion) and expressly deem the losses involved to be direct and therefore outside the scope of the exclusion or the cap.

Although a Contractor's indemnities are a standard carve out under Clause 17.1 (because these are insured losses), complex discussions often take place concerning the extent of that carve out. What if the Contractor does something that renders the insurance inapplicable and what about excess/deductible levels for the applicable policies?

All these and other issues frequently require extensive amendments to Clause 17.6.

The need for an exclusive remedies regime?

Express terms of contract do not operate in a vacuum and, if English law governs the contract, it may import rights, obligations and remedies. Because of this, provision is often added to FIDIC Silver for an 'exclusive remedies' regime. The effect is that the obligations of the parties are agreed to be exclusively and exhaustively set out in the contract, thereby excluding common law or other remedies. Contractors tend to require such a provision. Conversely, Employers tend to resist them.

A good starting point for the provision is Clause 44.4 of the IChemE Red Book (4th Edition), which has been endorsed by the English Court of Appeal.

Time periods for claims

The provisions for the making of claims under FIDIC Silver are one-sided.

Notice of claims by the Employer under Clause 2.5 has to be given "*…as soon as practicable after the Employer became aware of the event or circumstances giving rise to the claim*" but is not expressed as a condition precedent to the Employer's entitlement to proceed with the claim.

Notice of claims by the Contractor under Clause 20.1 also has to be given "*…as soon as practicable…*" but, additionally, "*…not later than 28 days after the Contractor became aware, **or should have become aware**, of the event or circumstances*" (emphasis added). The obligation to notify claims of which the Contractor ought to be aware may be seen as fruitful ground for negotiation and dispute.

Condition precedent

Also of concern to contractors will be the 28 day time limit, because, if the Contractor fails to give notice, "*…the Contractor shall not be entitled to additional payment, and the Employer shall be discharged from all liability in connection with the claim*". Under English law, this would usually prevent the Contractor from advancing a late claim, however valid.

Since contractors will frequently object to such a constraint a compromise solution is to replace the condition precedent with a tiered provision extending the periods for notifying and processing claims, perhaps with some ultimate cut off date and exclusion of liability if necessary details are not provided.

Alternatively, evaluation of the Contractor's entitlement could reflect late submission of the claim by taking into account the extent to which delayed submission impairs the Employer's ability to investigate, or to mitigate the effect of, the matters giving rise to the claim. Indeed, this type of device is employed in Clause 20.1 of FIDIC Silver.

The final paragraph provides that if the Contractor fails to comply with the requirements set out for notifying or substantiating its claims, then "*any extension of time and/or additional payment shall take account of the extent (if any) to which the failure has prevented or prejudiced proper investigation of the claim*". Equally, it has to be recognised that the outcome of such an exercise will often, if not always, be uncertain. This is because the breadth of the relief allows ample room for debate as to what impact non-compliance had on the ability to investigate; objective measurement is difficult to establish with any certainty. As noted, it would also be beneficial if the device referred to the impact on the Employer's ability to mitigate the effect of any matter as well as its impact on the ability to investigate a claim.

Early warning?

An Employer and its financiers will be keen to see that claims are managed proactively and that costs and delay overruns are reduced where possible. It may therefore be possible to agree to require the parties to give early warning to each other as soon as they become aware of matters that could affect the price, completion, performance or compliance with the Employer's Requirements and for the parties then to meet to consider proposals to deal with the effect of these matters and determine the action to be taken.

Similar provisions have been used on large infrastructure projects and are a feature of NEC3. They also make their FIDIC debut in the Gold Book.

Programme for Contractor's claims

In contrast to the 28 day cut off date for the Contractor's notice, the period between the initial claim event, the reference (if necessary) of the claim to a Dispute Adjudication Board and then (since reference to the DAB is a condition precedent) to arbitration is potentially lengthy (up to 126 days to reach the DAB and up to 294 days to reach arbitration plus the time taken for the Employer to reach a determination under 3.5*). In summary, the timetable is:

Step	Period
initial period for Contractor's notice	28 days
submission, by Contractor, of "*fully detailed claim which includes full supporting particulars of the basis of the claim...*"	14 days
Employer's response, with detailed comments (if not in agreement) and any request for particulars	42 days (or period proposed by Employer and agreed)
Determination under Clause 3.5*	
Contractor gives notice of dissatisfaction under 3.5	14 days
Contractor refers dispute to DAB under 20.4	
DAB appointed after notice to refer	28 days
	126 days
DAB decision	84 days
Notice of dissatisfaction and reference to arbitration	28 days
Amicable settlement period	56 days
	294 days

Unless both parties abide by the DAB's decision and arbitration follows (which, in a large or complex dispute, may be inevitable), the DAB reference may simply add unnecessary time and cost to the process. Some parties may find such a situation to be sufficiently unattractive to delete altogether the DAB process.

Conclusion

It is said that the outcome of negotiation of an EPC Turnkey contract depends on three main factors:

- the parties' bargaining strength;
- what is currently obtainable in the "market" for the particular sector for this type of agreement; and
- the negotiating skills and resources of the parties and their legal advisers.

Whilst all these propositions are true, the use of FIDIC Silver as the starting point for a turnkey contract is also to be commended. However, I would also suggest that FIDIC Silver (which FIDIC are intending to review in 2009) should always be subject to amendment. No one size fits all.

Jonathan Hosie

This is an abridged version of a paper delivered by the author at the FIDIC International Users' Conference in December 2007.

New IChemE forms for international use

A booklist with a difference. Red, green, burgundy and yellow, the new suite of "international" forms of contract recently published by the Institution of Chemical Engineers.

40 years ago the IChemE published its first contract, the Model Form of Conditions of Contract for Process Plants suitable for Lump Sum Contracts in the United Kingdom. From that beginning, the IChemE suite of contracts now consists (both domestic and internationally) of some ten contracts together with associated guides and dispute agreements.

The International forms

Published in October 2007, these comprise:

- International Red Book (lump sum)
- International Green Book (cost reimbursable)
- International Burgundy Book (target cost)
- International Yellow Book (subcontract)

As with all IChemE contracts, the new contracts deal with process plant and, to that extent, are a different breed from a standard building contract for construction works.

The international nature

IChemE have responded to the growing use of the IChemE forms outside the UK. This is due, in part, to the increase in the number of projects requiring process plant technology, particularly in emerging markets. In the words of the IChemE, they are "*committed to being a global player promoting best practice*". Those familiar with the previous editions of the IChemE forms will know that if those were to be used on projects taking place outside the UK, then certain UK legislative provisions in the contracts required amendment, for example, references to the Housing Grants, Construction and Regeneration Act 1996 which only applies where construction operations are being undertaken in England and Wales. Amendment was needed to remove such provisions. The international forms do not, therefore, contain any references to legislation of a specific jurisdiction.

A word of warning, however. Just because the contracts are labelled "*International*" does not necessarily mean that the contracts are suitable for use in any particular jurisdiction. As with all contracts, legal advice should be sought when looking to use the IChemE forms in a particular jurisdiction or indeed where one of the contracting parties is from outside the country where the project is taking place. Irrespective of what the contracts may say,

local law of that jurisdiction may be implied into the contract or certain provisions of the contracts may be incompatible with local law.

What does in fact make a particular contract 'international'? Other than removing provisions specific to domestic legislation, do the international forms differ greatly from their domestic counterparts?

Versatility

The IChemE has produced a suite of contracts to be used in a variety of procurement situations. Dictating the choice of contract is the method of payment, namely lump sum, reimbursable or target cost. In addition, the Yellow Book sub-contract is drafted to integrate with one of the main contracts. In terms of structure, the contracts comprise an Agreement, Conditions of Contract and Schedules.

The contracts rely heavily on the use and completion of the Schedules and it is important to ensure, when completing them, that the provisions are consistent, and do not conflict, with the remainder of the contract.

Key features

Sufficiency of contract price

Under clause 6.1 of the Red Book the contractor is:

"deemed to have obtained all information and taken account of all circumstances which may affect [the cost of executing the works] before agreeing to the Contract Price."

Whilst this may seem to transfer all of the risk to the Contractor, the clause also states it is "*subject to the provisions of the contract*" and there are various instances in the contract where the Contractor might be entitled to an increase in the Contract Price for certain occurrences (eg unforeseen ground conditions or incorrect purchaser data). Care also needs to be taken when completing the Schedules not inadvertently to allow the Contractor an increase where one is not intended.

Limitations on liability

The contracts contain certain limitations of liability, including an overall cap on liability and a limitation in relation to the types of losses that might be recoverable (eg loss of profit and wastage during the contractor's use of plant). Consideration will need to be given on a project by project basis as to whether the inclusion of such limitations is suitable and, if so, what an appropriate cap on liability might be.

Performance tests

The contracts contain provision for the inclusion of specific guarantees in relation to the performance of the plant. The detail of the performance testing regime and any liquidated damages associated with a failure to meet certain performance levels will need to be meticulously set out in the Schedules. It is very important that the terms of the Schedules are consistent, and integrated, with the provisions in the Conditions of Contract so that the overall performance testing regime is clear.

Variations

The Contractor may object to any variation ordered or proposed if compliance with it would, when combined with all Variations previously ordered, increase or decrease the Contract Price by more than twenty five percent. Employers may consider the deletion of this restriction.

Cooperation

The contracts contain a provision that the parties are to "*deal fairly, openly and in good faith with each other*". Just like the comparable provision in NEC3 it remains to be seen what effect this particular obligation might have if, and when, interpreted by the courts (of whichever country). Might it be interpreted as an overriding objective which sits above all other obligations in the contract and, if so, where does that take the parties?

Dispute resolution

The contracts contain an escalated dispute resolution procedure whereby any disputes are first to be determined by the project manager and subsequently by arbitration. Consideration may need to be given to whether some form of expert determination or dispute adjudication board is appropriate.

Successful formula?

It remains to be seen exactly how much the "*International*" contracts will be used outside the UK. The IChemE contracts remain, however, one of the few significant sets of process plant standard forms in the market and are therefore well placed to continue their rise in popularity. As with any contract, care should be taken when using the international forms in any particular jurisdiction.

Further information

For those interested in finding out more about the international forms, more details can be found on the IChemE website at www.icheme.org. In addition to hard copies of the international forms, the IChemE also produces electronic versions which are available to users on annual subscription.

Jonathan Olson-Welsh

Has FIDIC got the Midas touch?

It may not glitter but FIDIC has turned to gold. The new FIDIC Gold Book, released in September 2007 as a pre-press edition, is designed for use on design, build and operate projects where one entity (e.g. a consortium or joint venture) takes total responsibility for an engineering project incorporating the design, manufacture, delivery and installation of a facility and the long term operation and maintenance of that facility on behalf of the employer.

From the variety of possible DBO scenarios, FIDIC has adopted that of a *'green field'* DBO project with a 20 year operation period. Amendments will therefore be needed for different scenarios such as *'brown field'* operate-design-build projects or where the operation period varies significantly from the 20 year period. A Guide which includes details of the changes necessary for a *'brown field'* arrangement or a different operational period is to be published with the first Trial Edition this year.

Key features

The Gold Book generally follows the usual FIDIC format and uses familiar FIDIC terminology. The design and build element is similar to the Yellow Book (Conditions of Contract for Plant and Design-Build) with the operations element being new to FIDIC. There are flow charts included to explain the contract sequencing and procedures.

The Employer *must* appoint an Employer's Representative (as opposed to "may" under the Silver Book (Conditions of Contract for EPC Turnkey Projects)) who has a similar function to that of the Engineer under the Yellow Book.

FIDIC claim a number of advantages of using the Gold Book, including:

- the opportunity of overlapping some design and build activities making it possible to minimise delays and optimise the smooth flow of construction activities;
- a reduced risk of cost over-runs because cost restraints and commitments and other risks are carried by the contractor;
- because the contractor is responsible for 20 years operation, it has an interest in designing and building quality plant with low operation and maintenance costs. Not only will plant be *'fit for purpose'* but it will be built to last.

Since many of the conditions applicable to the design and build elements are taken from the Yellow Book (with some exceptions discussed later), the main additional advantage claimed is the last of the three cited. But does the machinery of the new contract live up to its gold star billing?

- Fixed price – including asset replacement

  Payment to the Contractor is on a lump sum/fixed fee basis and the Contract Price includes an Asset Replacement Fund. With its tender, the contractor submits an Asset Replacement Schedule setting out the identification, timing and cost of asset replacements. The Asset Replacement Fund is the total of the costs identified in the schedule and against which the Contractor is paid.

The Contractor bears the cost of replacing any assets not identified in the Schedule and any additional cost of replacing assets, where the cost is greater than the Schedule allowance. Any monies remaining in the Fund on completion of the contract are shared equally between Employer and Contractor.

A contractor tendering under the Gold Book will therefore need to ensure that its Asset Replacement Schedule is complete and contains adequate allowance for the replacements identified.

- Maintenance Retention Fund

  The Employer is entitled to deduct 5% from interim payments during the Operation Service Period (up to the value stated in the Contract Data) unless the parties replace this with a Maintenance Retention Guarantee. Where the Contractor has failed to carry out its maintenance obligations, the Employer can draw upon this fund in order to carry out the maintenance itself. The remaining retained funds are included in the final payment to the Contractor.

- Audit

  During the Operation Service Period an independent audit body (jointly appointed by Employer and Contractor) audits and monitors the performance of Employer and Contractor in compliance with the Operation Management System (the procedures and requirements for the proper implementation of the Operation Service). Although the audit body does not have power to issue instructions, the parties are required to give "*due regard*" to the matters raised by the auditing body in its report.

- Risk shuffling

  The risk and insurance conditions that were found in the previous FIDIC documents (such as the Yellow Book) have been updated and resequenced and the Employer's Risks have been divided into those applicable during the Design-Build Period and the Operation Service Period and further split into Commercial Risks and Risks of Damage. The Contractor's risks for the Operation Services Period have also been expressly described and include all risks resulting or arising from the Contractor's design or construction of the Works (and the Materials). This means, in theory, that the Contractor's responsibility for its work may last rather longer than under a traditional design and build contract.

- Early warning

  The Gold Book also introduces an early warning system (clause 8.4) whereby the Contractor and Employer are required to advise each other of circumstances which may increase the Contract Price, delay the works or otherwise adversely affect the works.

Aka force majeure?

This old favourite has been replaced with *'Exceptional Risks'* and the risk of forces of nature (which need to be specified in the Contract Data) occurring during the Design-Build Period has been allocated to the Contractor.

- Inspection before final handover

  A joint inspection by the Contractor and Employer's Representative is required at least two years prior to the end of the Operation Services Period and any works identified during the inspection (and in the Contractor's subsequent report) have to be undertaken by the Contractor over the remainder of the Operation Service Period. Tests prior to Contract Completion are also required towards the end of the Operation Service Period.

- Cut off date - game over?

  The Employer is entitled to terminate the Contract where the Contractor fails to complete the Design-Build by the Cut Off Date - which is at the end of the period specified in the Contract Data after the Time for Completion of Design-Build. If no period is specified the default period is 182 days.

- Late claims

  The condition precedent to claim entitlement found in the 1999 FIDIC documents, that the Contractor must have notified the claim within 28 days of becoming aware (or when it should have become aware), has been softened. The Dispute Adjudication Board can now override the condition where the late submission is considered "acceptable". What exactly is "acceptable" is, however, not explained.

DAB on call

The DAB is appointed by a date set out in the Contract Data instead of within 28 days of notification of a dispute, as was the case under the 1999 FIDIC documents. This development should speed up claim processing.

Gold rush?

Parties will need to think carefully about using the new Gold Book once the final version emerges. Like PFI and PPP (and marriage) 20 years plus is a big commitment for consortia funding a lump sum/fixed fee contract and one that no party can afford to get wrong.

Questions arising from the new formula are inevitable and so, therefore, are amendments. Detailed consideration will need to be given, not only to the terms of the Gold Book and any amendments, but also to the Employer's Requirements so that, for example, the Employer can retain some flexibility in output requirements (without having to instruct the same as a Variation each time) to suit its long-term needs.

Whether the Gold Book will ultimately prove a starting point for DBO projects remains to be seen. Winners generally have to prove themselves.

Monica Chaplin

The next best thing to a title?

And no, this is not about cash for peerages, this is about cash for property. Someone is building something for you but, before the product is finished and handed over so that you have title to it, someone else obtains judgment against the company producing it and puts the bailiffs in, to take possession of what you were paying for. So where does that leave you? Might you really be left without the product and have to say goodbye to all the money that you handed over for the work and materials involved?

Perhaps not, according to the intriguing case of ***International Finance Corporation v DSNL Offshore Limited***.

Chevron Nigeria Limited contracted with DSNL for the design, construction, transport and installation of rig modules and equipment to be fitted on to a Chevron rig platform in Nigeria in order to operate a water injection programme. Incorporated in the modules were turbine generators and pump sets purchased by DNSL from a US subcontractor for which, under a contract amendment, Chevron paid the subcontractor direct and arranged (and also paid) for delivery to DSNL. The generators and pump sets were delivered to DSNL and then attached by DSNL to two steel framework bases (known as pancakes) to which DSNL had title.

So far, so good, but life then became more complicated. IFC obtained summary judgment against DSNL for just under US$20,000,000 and the English High Court Enforcement Officer took possession of the modules and equipment. But Chevron needed to ship the modules and equipment from Middlesbrough (where they were being constructed) to Nigeria during a key period in the weather window, if oil production was not to be affected and which, it was said, would cause Chevron to incur "*very large losses*".

Chevron, which had paid its suppliers a total of US$36,337,000 (in contrast to the value of DNSL's work and materials which was no more than US$314,000) challenged the High Court Enforcement Officer's possession in the English High Court, claiming that it had title to the turbine generators and pump sets (and other equipment) by virtue of its agreement for direct payment to the US subcontractor, even though these items had been attached to the pancakes (to which DSNL had title).

The claim failed. Chevron, said Mr Justice Colman, did not have title. That had passed to DSNL on delivery by the US subcontractor and remained with DSNL. Chevron, however, had a Plan B. If it did not have title, it said, it had an equitable lien over all the equipment for which it had paid. The sum secured by the lien was the US$36,337,000 that it had paid for equipment and goods, under contract amendments, and for services.

Equitable liens usually appear in relation to sales of real estate in English law, where a vendor of real estate who has not been paid has a right in equity, once a binding contract has been made, to retain the property until payment has been made. This lien continues to exist even if the vendor executes a conveyance and parts with possession of the property and the title deeds. But did this equitable lien apply to Chevron's contract for work and materials with DSNL? Rig modules and equipment were not real estate.

Yes, it did, decided Mr Justice Colman. Chevron did have an equitable lien. Whether there was, or was not, an equity conferring priority over unsecured creditors depended, on the English authorities to which he referred, on the terms of the underlying contract and on the conduct of the parties in relation to it. Proceeding on the basis that the

contract was one for work and materials, it was impossible to exclude the availability of equitable relief in a case where the contracted work product and its components were to have characteristics specifically designed for the requirements of the purchaser.

Even if specific performance was not available, the Court of Appeal decision in ***Chattey v Farndale Holding Inc.*** had decided, said Mr Justice Colman, that an equitable lien may be enforceable by a different kind of equitable remedy (e.g. an injunction). Although the decision in ***Chattey*** was concerned with an agreement for the sale of an interest in land, Lord Justice Morritt in ***Chattey*** had referred, with apparent approval, to the decision of the majority of the High Court of Australia in ***Hewitt v Court.*** This was the only authority that could be found that dealt with the (successful) claim of a purchaser, under a contract for work and materials, to an equitable lien in respect of contractual prepayments before title to the completed property (a prefabricated home) had passed.

In ***IFC***, Mr Justice Colman had no doubt that, in principle, a lien arose on delivery of the equipment from the US (for which Chevron had made payment to the subcontractor) and the relevant equitable remedy would have been an injunction to restrain disposal of the equipment until, at the least, DSNL had reimbursed all relevant payments. Mr Justice Colman also found that the lien survived the attachment of the equipment to DSNL's own property (i.e. the pancakes). The practical result was that execution against the modules in respect of the judgment debt due to IFC could not be effected unless and until the lien had been discharged.

The case seems to be a first in English law in terms of applying an equitable lien to a contract for work and materials but the credit crunch climate may encourage its use. The catch, however, is the difficulty in knowing just when an equitable lien arises. It has been pointed out that they are not registrable, they do not arise under a contract and there does not seem to be a reliable test for identifying one. But then, the purpose of an equitable lien is, of course, to produce a fair result and prevent injustice. Which is, after all, why equity is there in the first place.

Richard Craven

Extras

ICC Model Turnkey Contract for Major Projects

FIDIC and IChemE are not the only ones to have issued new contracts. ICC recently launched the *ICC Model Turnkey Contract for Major Projects* for use in major projects. It is intended to provide contractors and employers:

"..with a unique, balanced platform that is fair to all parties. At the same time, the model accommodates the desire of all parties for price and scope certainty, the need for swift and effective dispute resolution, and the need for complete and informed allocation of risks."

For more details see: http://www.iccbooks.com/Product/ProductInfo.aspx?id=488

More in the next issue. And that's not all...

PPC International and SPC International

In October 2007 international versions of the ACA Project Partnering Contract, PPC2000, and the ACA Specialist Contract, SPC 2000, were published. PPC International was trialled in the Middle East, in particular on the University Hospital, Dubai.

For further details see: http://www.ppc2000.co.uk/PPC2000.htm

What's been happening at Mayer Brown?

It's been a memorable couple of months...

13 December 2007 – Brazil!

Much excitement, just before Christmas, as Mayer Brown officially opened its office in São Paulo, with Stephen Hood, who has extensive international experience, particularly in the Brazilian legal community, as the partner-in-charge.

Brazil is one of the world's fastest-growing financial markets, particularly with a surge in IPOs, infrastructure financing and cross-border acquisitions and Mayer Brown expects to add approximately a dozen lawyers in São Paulo over the next 18 months, complementing the firm's 40-strong Latin American practice group. The office will focus on foreign investment, infrastructure finance, debt and equity capital markets, structured finance, corporate transactions, debt restructuring and trade finance.

Contact information for Mayer Brown in São Paulo is:

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2 January 2008 – welcome to Chris Fellowes

And just after Christmas, in the January transfer window, so to speak, we were delighted to welcome Chris Fellowes on his return to Mayer Brown as a partner in our Construction & Engineering Group. Chris will be continuing the development of our construction practice in the support of projects from retail and commercial developments through to waste to energy plants and metropolitan rail schemes.

Chris has an impressive range of construction and engineering experience and skills, and not just as a lawyer. Before qualifying as a solicitor in 1997 Chris practised as a Chartered Quantity Surveyor and as a Project Manager and was also the Development Director of a property development company.

With his lawyer's hat on, Chris has acted for all the sides of the industry - developers, employers, consultants, funders, tenants, investors, contractors and sub-contractors on a mixture of construction and engineering projects, PFI/PPP agreements, facilities management and maintenance contracts. Whilst most of Chris's work is non-contentious, he has also been involved in a number of adjudications, arbitrations, High Court actions and mediations.

Welcome to the team, Chris.

7 January 2008 – congratulations to Nick Henchie

Nick Henchie, one of our Construction & Engineering Group partners is listed in The Lawyer's Hot 100 survey, 2008, as one of 100 lawyers to have excelled in their field during 2007. The Hot 100 survey celebrates individuals in all areas of the legal profession in particular those who have enhanced the reputations of law firms, chambers, organisations or companies.

Nick joined Mayer Brown in 1993 and was promoted to partner in 2003. His work ranges from front-end procurement and contract strategy (including the drafting and negotiating of major construction contracts), to claims and dispute management of construction and engineering projects - particularly in the petrochemical, mining and power generation/energy sectors all over the world.

Nick has been involved in a wide range of international disputes and arbitrations under the ICC and LCIA rules and various ad hoc rules in relation to construction projects in Singapore, Hong Kong, St. Lucia, Saudi Arabia, Indonesia, Jordan, India, Egypt, Qatar, the Caspian Sea and a number of European countries.

He has particular FIDIC expertise, having advised many clients on amendments to standard forms and he has lectured and written extensively on FIDIC contracts, in part reflecting his former role as Chairman of the International Bar Association Committee on FIDIC contracts. Nick was also retained in 2007 as procurement Counsel to the Panama Canal Authority in relation to the high profile US$5.2 billion Panama Canal Expansion Programme.

28 January 2008 – welcome to Johnson Stokes & Master

28 January 2008 was another big day as it marked the combination of Mayer Brown and Johnson Stokes & Master (JSM), a leading Asian law firm.

The combined firm has 21 offices round the globe - seven in Asia, six in Europe and eight in the Americas with more than 1,000 lawyers in the United States, 500 in Europe and 300 in Asia. No other law firm can provide this level of coverage; the Mayer Brown JSM combination provides a solid platform for the firm's clients, from multi-national corporates to financial institutions, to access quality legal services and support for their business ventures. The Construction & Engineering Group expect to play a major role on infrastructure and developments, energy, petrochemical and transportation projects in the region.

Established in 1863 in Hong Kong, JSM is one of the oldest and largest law firms in Asia with full-service offices in Hong Kong, mainland China (Beijing, Guangzhou and Shanghai), Thailand (Bangkok) and Vietnam (Hanoi and Ho Chi Minh City). It has a multinational, multilingual team of 800 staff, including more than 260 lawyers who are qualified in local and international jurisdictions and has been named Hong Kong Law Firm of the Year for the past eight years (2000-2007) by various leading legal publications, including International Financial Law Review, Asian Legal Business and Who's Who Legal. JSM is also one of the top three foreign law firms in Thailand and Vietnam.

JSM's Construction Group acts for developers, Government and other public institutions, utility and transport undertakings, consultants, contractors and insurers on all aspects of building and civil engineering contracts in Hong Kong, Mainland China and the rest of Asia.

The combined firm will continue to be known as Mayer Brown outside Asia. In Asia, it will be known as Mayer Brown JSM.

And on the UK front...

CIC Consultants' Contract arrives

Another contract for the grown-ups? First it was the Major Project Form; now it's the CIC Consultants' Contract. For use by experienced users on major building projects, the CIC's new package can be used for appointments of any discipline.

Said to contain no surprises or gimmicks and to be very simple and straightforward, it is not seen as a rival to the RIBA forms but does put some pressure on the BPF Consultancy Agreement.

Like the Lord of the Rings, it comes in three parts – conditions, scope of services and services handbook and is intended to resemble a negotiated compromise, striking a balance acceptable to institutions and insurers.

The freestanding services document, that can be used with other contracts, seems likely to attract the most attention. Apparently put together by a team of 10 construction practitioners, it is intended to record what everybody does on a construction project so that all the tasks can be allocated (on line or in hard copy) to all the relevant people.

Features

- the defined standard of care is that of the experienced consultant;
- no net contribution clause in the conditions but there is a cap on liability and a sample net contribution clause, if required;
- a Third Party Rights Schedule, based on the CIC form of warranty, which does have a net contribution clause;
- notification of a claim for additional fees within the contract timescale is a condition precedent to recovery;
- instead of talking in terms of design and construction, the scope of services refers to the "definition process" and construction, design being just one of the elements of the definition process (with management, co-ordination, costing etc.);
- it is anticipated that the package will be used outside the UK.

Take a look and see what you think, at:

http://www.cicshop.co.uk/acatalog/CIC_Consultants__Contract.html

Richard Craven

Planning law changes

Goodbye PGS but hello PRB. The proposed planning gain supplement (see issue 53) is dead. The proposals previously reported were for a new supplement to be paid by developers when they commenced the development of land, as a levy on the '*uplift*' in the value of the land which accrues when planning permission is granted to carry out development. Following a lengthy period of consultation, the Government announced towards the end of 2007 that it would not now introduce this new tax.

While this will be a welcome announcement for developers and land owners alike, this is not the end of the matter. The Government remains committed to its belief that "*it is right and fair that local communities should benefit more from uplifts in land value arising from planning permission to finance the infrastructure needed to support housing growth*", and it has announced that it will "*legislate in the Planning Reform Bill to empower local planning authorities in England to apply new planning charges to new developments*", which will be in addition to s106 agreements.

Details of the new statutory charge are sparse at the moment, but it has been stated that "*planning charges should be based on a costed assessment of the infrastructure requirements arising specifically out of the development contemplated by the development plan for the area…taking account of land values*".

The new statutory charge will be introduced after a period of consultation and evaluation and there is not yet any stated commencement date. For more details on the proposed statutory planning charge see

http://www.communities.gov.uk/statements/corporate/planningreform.

Jane Feeney
Corporate Tax Group

Ignore the protocol...

At your peril. Two recent cases have underlined the importance of complying with the Construction and Engineering Pre-Action Protocol.

Charles Church Developments v Stent

CCD brought proceedings against Stent without first complying with the pre-action protocol. The claim related to events which had occurred nearly six years beforehand and CCD started the proceedings because it was concerned about limitation issues.

Stent served its defence and raised objections to CCD's failure to comply with the protocol. It argued that it had been forced straight into the higher cost arena of formal proceedings without first being given an opportunity to try and resolve the dispute in the lower cost arena of the protocol.

The judge was sympathetic to Stent's argument and decided that, when CCD served its proceedings, it should simultaneously have sought directions for an immediate stay to enable the parties to comply with the protocol. Its failure to seek such directions resulted in it being hit with a substantial adverse costs order.

And so to..

Cundall Johnson and Partners v Whipps Cross University Hospital NHS Trust

where a similar issue arose. CJP brought proceedings to recover unpaid professional fees without first complying with the protocol.

The Trust asked for details of CJP's claim. CJP failed to provide the details and requested a meeting but the Trust refused to meet until proper details of CJP's claim had been provided. CJP commenced proceedings.

The Trust sought an order that the proceedings should be stayed because CJP had not complied with the protocol.

The Judge decided that the protocol requires each party to provide a clear and concise summary of its case but both parties should take a proportionate approach – letters of claim and responses are not required to be so detailed as to resemble pleadings. As CJP had failed to comply with the protocol, the judge ordered an immediate stay.

Matthew Olorenshaw

The new corporate manslaughter legislation - what you need to know

The Corporate Manslaughter and Corporate Homicide Act 2007 comes into force on 6 April 2008.

What does the Act do?

- it introduces a new offence of "*corporate manslaughter*", which will sit alongside existing health and safety legislation;
- the Act applies to an "*organisation*" which includes companies, partnerships and other bodies. It focuses on the organisation itself and does not impose new sanctions on individual directors or managers;
- the offence is directed at the management, policies and practices of the organisation, rather than individual operational shortcomings;
- an organisation will be guilty of corporate manslaughter if the way in which any of its activities are managed or organised causes a person's death and amounts to a *gross breach* of a relevant duty of care owed by that organisation to the deceased;
- an organisation commits a *gross breach* where it has fallen "*far below what can reasonably be expected of the organisation in the circumstances*". Systemic failure to comply with legislation will be a significant factor in determining whether there has been gross breach.

What is the penalty for corporate manslaughter?

- The maximum penalty is an unlimited fine. Fines are likely to be set at a high level to match the seriousness of the offence;
- the organisation can be ordered to take remedial steps to deal with any deficiency in its policies or practices;
- the court can order that the conviction, particulars of the offence, the level of fine and any remedial steps are publicised.

What practical steps should be taken?

- Ensure that the organisation's management has put in place appropriate health and safety systems and procedures;
- ensure that they are routinely followed and that they are regularly reviewed to see that they remain "*fit for purpose*";
- check whether existing insurance covers defence costs and consider whether further cover is required.

Stuart Pickford

The all weather arbitration clause

English law arbitration clauses will now fit all disputes. This is the news from the House of Lords in ***Fiona Trust & Holding Corporation v Yuri Privalov: Premium Nafta Products v Fili Shipping.***

Recognising the "*rational commercial purpose*" of agreements to arbitrate, their Lordships held that the construction of an arbitration clause had to start from the presumption that the parties, as rational businessmen, intended that any dispute arising out of an agreement or alleged agreement to which the clause relates should be decided by the tribunal which they had chosen.

They recognised that, particularly in international contracts (such as the FIDIC forms discussed elsewhere in this Update) the parties want a quick and efficient determination of the dispute and do not want delay or (as can happen in some jurisdictions) partiality by the local courts.

Two issues arose in the case:

- as a matter of construction, was the arbitration clause apt to cover the question of whether the contract was procured by bribery?
- is it possible for a party to be bound by a submission to arbitrate when it alleges that, but for the bribery, it would not have entered the contract containing the arbitration clause?

On the first issue, their Lordships held that the arbitration clause should be construed in accordance with the presumption identified above, unless the language of the clause makes it clear that certain questions are intended to be excluded from the arbitrator's jurisdiction. They emphasised that a line should be drawn under previous authorities which sought to find a distinction between words such as "*arising out of*" and "*arising under*" the agreement and that only clear express wording to the contrary would rebut the presumption that the dispute should fall within the scope of the arbitration clause.

On the second issue, their Lordships reaffirmed the principle of separability in S7 of the Arbitration Act 1996. The arbitration agreement must be treated as a distinct agreement and is voidable only on grounds which relate directly to the arbitration agreement as opposed to the underlying contract.

The decision represents a clear statement of intention by the English Courts not to interfere with the commercial rationale behind agreements to arbitrate. This should encourage parties to international contracts to select English law as the law of the arbitration.

Whilst not free from doubt, it is also likely the decision will be interpreted as applying not just to international arbitrations but to those conducted nationally. The determining presumption is that a businessman, whether national or international, intended all disputes to be resolved under the arbitration agreement.

Tom Duncan

Rearranging your appointments?

Autumn 2007 brought a lot of new appointments. Seven from the RIBA (see Update 54), not to mention the CIC form discussed elsewhere in this Update. Taking the new Standard Agreement 2007 S-Con-07 for the appointment of an Architect (son or daughter of SFA/99) as an obvious sample, just how useful are the changes from SFA/99?

The form looks a little different (but is still blue). What is different, and may cause a practical problem, is that all the new hard copy agreements are in bits (literally). Binding them together and striking out unwanted sections might save later frantic searches for vital missing ingredients.

The 2007 edition (separate) Conditions are divided into Part A, which applies to all Clients, and Part B, which deals with adjudication and the Construction Act provisions, and is not intended to apply where the Client is a consumer, unless the Client decides otherwise.

Perhaps the most significant change is that the Architect has more obligations under the 2007 edition. These include an express duty on the Consultant to comply with the Client's brief or any timescale or cost limit, "s*o far as is reasonably practicable*". The qualifying words have been said to dilute the Consultant's obligations but, elsewhere, it has been suggested that, although reasonable skill and care is the standard to be achieved in carrying out these additional obligations, the Agreement could have created strict, or fitness for purpose, obligations. Whichever is correct will not be good news for one of the parties.

There is provision for a third party rights schedule and a Consultant switch or novation. There has also been some (though limited) concession to clients. The contract interest rate for late payment has been reduced from 8% to 5% over bank base rate and the indemnity given by the Client to the Architect has disappeared.

Clients will, however, still be concerned by (and their Consultants pleased to see) no change on most of the old familiar issues, such as:

- the cap on liability and optional net contribution clause;
- the copyright licence conditional on payment of fees; and
- exclusion of all the client's rights of set off.

All in all, however, is this a missed opportunity to take a more balanced approach, as in the new CIC form?

Ruth Wilkinson

Holding it all back...

Rarely has there been so much hype for a Construction Act case. Articles were written (see update 54), seminars were arranged and all asking the same question –was the House of Lords' decision in ***Melville Dundas v George Wimpey*** only relevant to insolvency cases or did it open the floodgates for paying parties to get round the fact that no (valid) withholding notice had been issued?

The decision was soon tested in ***Pierce Design International v Mark Johnston and Another***. Mr and Mrs Johnston entered into the same form of contract as in *Melville Dundas* and appointed Pierce Design International as contractors. Five interim valuations were issued and, in respect of each one, a lesser sum was paid by the Johnstons without issuing a withholding notice. The overall shortfall was some £93,460.33.

Some months later the Johnstons purported to determine Pierce's employment. Pierce commenced adjudication proceedings, seeking payment of the shortfall in respect of the five valuations and arguing that the sums had been "*unreasonably not paid*". The Johnstons tried to rely on the subsequent termination of Pierce's employment to say that, by virtue of *Melville Dundas*, it was entitled not to pay the money, despite the absence of withholding notices. They said that "*unreasonably not paid*" should be looked at in the present context (i.e. after the determination) and not what was unreasonable at the time payment was due.

Judge Coulson disagreed; the court needed to look at whether or not something had "*unreasonably*" not been paid when it fell due. To do otherwise would have allowed the Johnstons to rely on an earlier breach of non payment by simply determining Pierce's employment, and this would not have been a satisfactory position.

Which suggests that ***Melville Dundas*** is limited to cases of insolvency, but we may not know for sure until some suitable Construction Act amendments eventually reach the statute book. And that, of course, is another story.

Emily Monastiriotis

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A number of readers already receive this Update by email. If you would prefer to receive it by email, instead of a copy in the post, please contact us by post or by email to businessdevelopment@mayerbrown.com who will arrange this for you.

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