MAYER • BROWN

Construction & Engineering London Legal Update
March 2011

Construction & Engineering London Legal Update

Page

1. In this issue.

1. International arbitration:

  - The case of the disappearing respondent;
  - The evolution of arbitration in India;
  - Arbitration in the Middle East – new edition of the Guide;
  - Arbitration in India – a new Guide.

10. Don't go OTT in your NDA for an ITT.

12. Competition Appeal Tribunal slashes OFT cover pricing fines.

15. Extras.

19. Consultant passes Sandwich supermarket test.

21. How substitutions can change the employment game plan.

22. Has time been called on corporate hospitality?

23. PFI and procurement review:

  - Is PFI an endangered species?
  - And is there an alternative?
  - Why PFI contractors should be grateful for human rights law;
  - How to spend billions...
  - ...and save billions - PAS 91;
  - Challenging a public procurement award – when does the clock start ticking?
  - Supreme Court green light for local authority mutual insurance arrangements;
  - Look on the bright side – but not too much?
  - Pain in Spain – for the procurement laws.

35. What's been happening @ Mayer Brown.

36. Concurrent delay – Scottish and English courts part company.

38. If your US client or customer goes bust – don't make it worse.

39. RIBA 2010 Appointments – the changes in a nutshell.

40. Case notes.

In this issue

Welcome to issue 61 of the Construction & Engineering Update.

With the Government keen to promote growth it will be no surprise that PFI and procurement feature in this Update. Is PFI on its way to extinction and, if so, what is to take its place? Wisam Sirhan looks at where it could all be heading and why optimism might not be such a good thing in project planning. Sarah Byrt has some important advice to give on non-disclosure agreements and the Court of Appeal has found that human rights law can protect PFI pricing information – and yes, you did read that correctly. We are also delighted to have a report from Pablo Silván, a partner in our Alliance firm, Ramón y Cajal Abogados, in Madrid, on the problems that Spain has been having with its procurement law regime.

Arbitration in the international arena also features. Raid Abu-Manneh and Wisam Sirhan analyse the Supreme Court's decision in *Dallah Real Estate and Tourism Holding Company v Government of Pakistan* but we still have to wait for it to give its verdict on the Court of Appeal's controversial decision in *Nurdin Jivraj v Sadruddin Hashwani* (with the hearing scheduled for 6 and 7 April). Raid and Rebecca Downing explore the evolution of arbitration in India and we have details of a new edition of the Quick Reference Guide to arbitration in the Middle East and of a new Guide to arbitration in India.

Chris Fisher highlights the tricky issue of distinguishing workers and the self-employed in the construction industry, Gillian Sproul has the latest legal news on the OFT and cover pricing in the construction industry and Andrew Legg and Susan Rosser sound the alarm bells on corporate hospitality – the Bribery Act comes into force on 1 July. Andrew Shaffer and Jeremy Snead have some words of warning for those with US clients and customers and Chris Wright takes a look at the 2010 RIBA agreements. And, to complete the issue, we examine the latest (conflicting) law on concurrent delay and delegation (or not) of a consultant's duties to a specialist and round up the cases.

International arbitration

THE CASE OF THE DISAPPEARING RESPONDENT

Without effective enforcement, international arbitration can be pointless. The New York Convention, or the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958, to give it its full title, is there to provide that option. Widely recognised as the foundation instrument of international arbitration, it is the means by which international arbitration awards are given teeth in almost 150 countries around the globe. In ***Dallah Real Estate and Tourism Holding Company* v *The Ministry of Religious Affairs, Government of Pakistan***, however, this policy hit a fundamental problem. The Supreme Court's decision delivered a stark reminder that, to achieve enforcement, there must be a valid arbitration agreement.

In England, Wales and Northern Ireland, sections 100 to 103 of the Arbitration Act 1996 implement the Convention. S.100 defines a "New York Convention award" as an award made pursuant to an arbitration agreement in the territory of a state which is

a party to the Convention. S.101(1) emphasises that the enforcement of a Convention award is mandatory subject to limited and exhaustive exceptions which are specified in S.103 (2) and provide a high threshold for denying enforcement, including the incapacity of a party to an arbitration agreement, invalidity of the arbitration agreement and the award being contrary to public policy. The onus of proving such exceptions rests upon the party opposing enforcement and it is not for the claimant to demonstrate that an award does not contravene the Convention.

The 1996 Arbitration Act demonstrates a clear policy in favour of the enforcement of Convention awards, a policy which is reflected in the decisions of the English courts, including *Norsk Hydro ASA v State Property Fund of Ukraine* [2002] EWHC 2120 (Comm), where the court said that:

"...there is an important policy interest, reflected in the country's treaty obligations, in ensuring the effective and speedy enforcement of ... international arbitration awards".

That policy is not, however, without its limits, as the Dallah case demonstrated.

THE DALLAH CASE

Dallah agreed to provide housing for Muslim pilgrims who wished to undertake the Hajj. Initial negotiations took place between Dallah and the Ministry of Religious Affairs, and a memorandum of understanding was signed by Dallah and the Government of Pakistan in 1995.

It appears, however, that the agreement containing the arbitration clause which required disputes to be referred to an ICC arbitration in Paris, was entered into between Dallah and an entity known as the Awami Hajj Trust and, in December 1996, following a change of government in Pakistan, the Awami Hajj trust ceased to exist as a legal entity. Dallah subsequently commenced an ICC arbitration against the Government of Pakistan, seeking compensation.

Dallah appointed Lord Mustill as its arbitrator and the ICC under its rules appointed Justice Dr Nassem Hasan Shah to act as the Pakistani Government's arbitrator, with the highly respected Lebanese arbitrator Dr Ghaleb Mahmassani to chair the tribunal. In its first partial award, the arbitral tribunal held that the Pakistani Government was a true party to the agreement and, as such, should be bound by the arbitration clause. The arbitral tribunal subsequently rendered the final award in 2006 in which it ordered the Pakistani Government to pay approximately US$20.5million to Dallah.

Dallah sought to enforce the final award in England but the High Court refused enforcement on the grounds that the Government was not a party to the arbitration agreement. This decision was subsequently upheld by the Court of Appeal, and Dallah then appealed to the Supreme Court.

The Supreme Court considered whether recognition of enforcement should be refused on the grounds of s.103(2)(b) of the Arbitration Act:

"...if the person against whom it is invoked proves...(b) that the arbitration agreement was not valid under the law to which the parties subjected it or, failing any indication thereon, under the law of the country where the award was made".

Contrary to the findings of the arbitral tribunal, the Supreme Court found that there was no *"common intention"* that the Government of Pakistan would be party to the agreement, and therefore as a matter of French law (the law of the seat of the arbitration) the Government was not a party to the arbitration agreement providing for ICC arbitration in Paris. On this analysis, the Supreme Court's decision was that the Government had successfully demonstrated that the alleged arbitration "agreement" with it was *"not valid"* for the purposes of s.103(2)(b) of the Arbitration Act 1996.

THE EFFECT OF DALLAH

The headline message from the decision is that the English courts will not hesitate to intervene and deny enforcement under the New York Convention in circumstances where they do not believe that a valid arbitration agreement exists.

But also note the following aspects of the decision, when dealing with the enforcement of a New York Convention award:

- Dallah contended that the enforcing court, when faced with a decision by the tribunal that it has jurisdiction, should only conduct a limited review and cannot review the merits of an award *de novo*. Dallah also argued that a rehearing of the issue was a matter for the supervisory court and not for the enforcing court.

  Lord Mance disagreed, saying that: *"The tribunal's own view of its jurisdiction has no legal or evidential value..."*. Lord Collins also emphasised that a party can challenge jurisdiction in the courts of the arbitral seat; and it can also resist enforcement in the court before which the award is brought for recognition and enforcement. These options were *not* mutually exclusive although "... *in some cases a determination by the court of the seat may give rise to an issue of estoppel or other preclusive effect in the court in which enforcement is sought"*.

- Dallah argued, as a fallback position, that the word *"may"* in s.103(2) provided discretion for the Court to enforce the award even if the Court finds that there was no arbitration agreement.

  Lord Mance rejected the argument, saying: *"Absent some fresh circumstance such as another agreement or an estoppel, it would be a remarkable state of affairs if the word "may"* [in S.103 (2)] *enabled the Court to enforce or recognise an award which it found to have been made without jurisdiction, under whatever law it held ought to be recognised and applied to determine that issue"*.

Whether the case opens the floodgates for challenging the enforcement of foreign awards remains to be seen but, in the meantime, from a practical perspective, the Supreme Court's decision highlights the importance of parties ensuring that all entities with whom they are negotiating sign up clearly to an agreement so as to avoid future arguments on jurisdiction. Alternatively, parties should consider obtaining additional security from a parent company or from the relevant government itself.

Raid Abu-Manneh
RAbu-Manneh@mayerbrown.com

Wisam Sirhan
WSirhan@mayerbrown.com

Construction & Engineering Group (UK)

The evolution of arbitration in India

PAINTING THE PICTURE

Despite the recent downturn in the global economy, companies have continued to expand into emerging markets. One such emerging market, gaining ever-increasing popularity, is India. Much of the growth in business activity in India relates to foreign corporations investing into India, but the action is by no means one-sided: Indian corporates have been aggressive in pursuing projects and acquisitions overseas. It is unsurprising that this has led to the parallel development of a growing number of commercial disputes being fought on Indian soil or against Indian companies in an international environment.

Unfortunately India's already overburdened courts have not been able to keep up. There is currently a backlog of almost 30 million cases in the Indian judicial system, resulting in endemic delays in bringing commercial disputes to a conclusion. Litigating in India is therefore hardly an attractive option for corporations seeking speedy resolution of their disputes and arbitration has become of pivotal importance for businesses operating in India as well as those doing business with Indian entities.

In practice, however, arbitration in India has been marred by a number of significant shortcomings and unhelpful loopholes. This is a brief exploration of the evolution of domestic and international arbitration in India, uncovering the good, the bad and the ugly.

INDIAN ARBITRATION LEGISLATION

Commercial arbitration has been recognised as a mode of dispute resolution in India since at least 1840. The growth of domestic arbitration has been followed by the recognition of international arbitration by the courts and in statutes. The Indian Constitution itself provides as part of the directive principles of its State Policy (guidelines for the central and state governments in framing laws and policies), that the state will endeavour to encourage settlement of international disputes by arbitration. In keeping with this policy, in July 1960 India acceded to the 1958 New York Convention (the UN Convention on the Recognition and Enforcement of Arbitral Awards).

The then prevailing arbitration legislation, the Arbitration and Conciliation Act 1940, did not, however, reflect the general positive attitude towards settling disputes by arbitration. It dealt only with domestic arbitration and provided for court intervention before, during and after the arbitration.

Court intervention was required to start the arbitration and to extend time for making an award and the 1940 Act permitted courts to set aside an arbitral award where "*the award [had] been improperly procured or [was] otherwise invalid*". Indian courts interpreted this as allowing them substantively to review the merits of an award and to set it aside if it suffered from an "*error*" of law apparent on the face of the award. The 1940 Act consequently became a vehicle for disgruntled losing parties to challenge awards on the merits and, effectively, to re-try their cases before the Indian courts.

In January 1996 India enacted replacement arbitration legislation, the Arbitration and Conciliation Act 1996. The 1996 Act, based on the UNCITRAL model law, is considered a vast improvement on the 1940 Act and was designed to bring Indian arbitration law into line with international practice. The intention was to rectify the problems caused by the 1940 Act by minimising the supervisory role of the courts so as to ensure finality of arbitral awards and expedite the arbitration process.

OLD WINE IN A NEW BOTTLE

Unfortunately the sweeping changes brought about by the 1996 Act were entirely at odds with fifty-six years' worth of case law. The 1996 Act was also enacted following limited consultation and with little guidance as to how it should be applied. Consequently, in the absence of established case law and a general understanding of the 1996 Act, several provisions of the 1996 Act were interpreted by the Indian courts in their accustomed interventionist manner. The 1996 Act has therefore been referred to as 'old wine in a new bottle'.

The best known example of this approach is ***ONGC v Saw Pipes Ltd*** 2003 [5] SCC 705 where an Indian arbitral award was challenged on the basis that it was "*in conflict with the public policy of India*". Although precedent suggested that "*public policy*" should be interpreted restrictively and that a breach of "*public policy*" is more than a mere inconsistency with Indian law (see ***Renusagar Power Co. Ltd v General Electric Co***. (1994 Supp 1 SCC 644)), the Supreme Court of India interpreted "*public policy*" in the broadest terms possible, ruling that an arbitral award that violates Indian law is "*patently illegal*" and therefore contrary to "*public policy*" and unenforceable.

Venture Global Engineering v Satyam Computer Services Limited (2008 [4] Scc 190) is another example, where the Supreme Court considered an application to set aside an arbitral award made in London. In most jurisdictions such an application would fail, on the basis that an award may only be challenged in the jurisdiction in which the arbitration took place (i.e. London). The Supreme Court ruled, however, that foreign awards may be challenged under Part I of the 1996 Act (applicable only to domestic arbitrations and awards) unless the parties have specifically agreed otherwise (following its earlier decision in ***Bhatia International v Bulk Trading SA*** (2002 [4] SCC 105)). The Court also held that, when considering such a challenge, the Indian courts should apply the expanded definition of Indian "*public policy*", i.e. that an award can be set aside if it contravenes any substantive provisions of Indian law, thus affirming ***Saw Pipes***. ***INDTEL Technical Services v WS Atkins Rails Limited*** (2008 [10] SCC 308) is also significant because it decided that the Indian courts may still appoint an arbitrator in offshore arbitrations, unless Part I has been *expressly* excluded.

More recently, in ***Citation Infowares v Equinox Corporation*** (April 2009), the Supreme Court upheld an application to appoint a former Chief Justice of India as the sole arbitrator in a dispute under an agreement governed by California law, reaffirming ***Bhatia International*** and ***Venture Global Engineering***. The parties had agreed to arbitrate disputes under their agreement, but the arbitration's seat and the applicable procedural law had not been agreed.

Similarly, in ***TDM Infrastructure Private Limited v UE Development Private Limited*** (MANU/SC/2263/2008), the court held that a dispute between two contracting parties incorporated in India (irrespective of whether they are wholly foreign controlled and owned) represents a "*domestic arbitration*" for the purposes of the 1996 Act. On a broad interpretation this means that, under section 28 of the 1996 Act (applicable to domestic arbitrations), foreign investors conducting their India-related business through Indian incorporated entities are obliged to apply Indian law as the substantive law of the contract, regardless of the parties' choice of law, and even in circumstances where any disputes will be resolved by offshore arbitration. Crucially this means that the Indian courts could refuse to enforce an award rendered in a dispute between two Indian parties by an offshore arbitral tribunal, where the substantive law applied in accordance with the governing choice of law clause was not Indian law. Any victory in this scenario could therefore be short-lived!

So, should parties to a contract connected with India, who wish to avoid any Indian court intrusion into resolution of any potential disputes, always expressly exclude Part I of the 1996 Act? In ***Bhusan Steel Limited v Singapore International Arbitration Centre***, the Delhi High Court refused to exercise jurisdiction in a dispute relating to international arbitration on the ground that the provisions of the 1996 Act were excluded (both expressly and implicitly) and in ***M/S Dozco India P. Ltd. V M/S Doosan India***, the Indian Supreme Court refused to appoint an arbitrator in an international arbitration on the ground that the arbitration agreement excluded the application of Part I of the 1996 Act. Although in ***Dozco*** the Supreme Court seemed to suggest that an express exclusion is not required, and that it is enough if the applicable law is foreign law and the seat of arbitration is outside India, it is still advisable to include an express exclusion to ensure that the Indian Courts do not have jurisdiction.

Another example of undue judicial intervention is ***SBP & Co v Patel Engineering*** (2005 [8] SCC 618) which involved the appointment of an arbitrator by the Supreme Court Chief Justice after the parties' chosen method for constituting the tribunal had failed. The Supreme Court ruled that the Chief Justice was entitled to adjudicate on preliminary issues such as the validity of the arbitration agreement, and could call for evidence and resolve jurisdictional issues. It also held that any of the Chief Justice's findings on these issues would be final and binding. So much for the well-established principle of *kompetenz kompetenz* – the power of an arbitral tribunal to decide on its own jurisdiction.

More recently the Supreme Court, relying heavily on ***SBP***, held in ***Alva Aluminium Ltd*** and ***A.P. Tourism Development*** that, once the validity of the arbitration agreement is questioned, the issue has to be determined by the court or its designate. Again, this flies in the face of section 16 of the 1996 Act which says that the arbitration tribunal has the authority to decide on its own jurisdiction.

More encouraging, however, is the Supreme Court's recent decision in ***Indian Oil Corporation Ltd & others v M/S Raja Transport Pvt. Ltd*,** where it refused to interfere with an arbitration agreement in circumstances where the parties' chosen mechanism for appointing an arbitrator had failed. Instead, it ordered that the parties themselves appoint an independent arbitrator to rule on the dispute.

On balance, judicial intervention under the 1996 Act is still reasonably common. This may be because of scepticism about arbitration as an effective method of dispute resolution or concern that the courts' jurisdiction will be eroded. Whatever the reason, vigilant corporations undertaking business in India are well advised to adapt their contracts accordingly and pay particular attention to the drafting of their dispute resolution clauses.

THE LIGHT AT THE END OF THE TUNNEL

Setting arbitration-unfriendly precedents is obviously harmful to India's overriding aspiration to be a trusted international hub for arbitration, but all is not lost. Recent developments look set to improve the arbitration environment in India, making it a more attractive option for corporations.

The Indian Ministry of Law and Justice has recently published a consultation paper which proposes far-reaching amendments to the 1996 Act. The arbitration-unfriendly decisions noted above have raised questions about India's commitment to arbitration and prompted demands for reform. The consultation paper recognises gaps in the current arbitration framework and the 1996 Act, and observes that the interpretation of the 1996 Act in subsequent judgments has in certain cases "*defeated the main object*" of the legislation.

Notable proposals in the consultation paper include:

- a clearer definition of "*public policy*" as a ground for refusing enforcement of a foreign arbitral award. This proposal aims to nullify the extension of the courts' power under this heading;
- restricting the application of the 1996 Act to cases where the place of arbitration is in India. This proposal is intended to insulate arbitrations outside India from interference by the Indian courts;
- a greater role for arbitral institutions in the appointment of arbitrators;
- stricter timelines in arbitration; and
- making institutional arbitration mandatory for "*high-value disputes*" unless expressly excluded by the parties in writing. This proposal is highly controversial, given the well-established principle of the parties' freedom (or not) to choose arbitration.

The consultation paper has, understandably, been well-received by the legal profession but it is currently unclear when new legislation may be put before Parliament. An amendment bill was actually placed before the Indian Parliament in 2003, following a 2001 Law Commission paper, but the bill was subsequently withdrawn.

The absence of credible, efficient, Indian arbitral institutions has long been perceived to be a major drawback to arbitration in India. The vast majority of arbitrations in India are conducted on an ad hoc basis as opposed to being administered by an arbitral institution. The disadvantage of ad hoc arbitrations is that they are administered in accordance with the 1996 Act, so giving rise to the judicial interference we have seen above. The advantages of institutional arbitration, on the other hand, include the automatic incorporation of a set of tried and tested rules,

provisions dealing with the more sticky situations (for instance where defending parties are unwilling to arbitrate or refuse to appoint an arbitrator), and trained staff to administer the arbitration. In addition, some of these rules already have an international dimension, since they are not linked to a particular national law.

It is good news therefore that the LCIA launched its India centre in April 2009, in an attempt to plug the gap caused by the lack of Indian arbitral institutions. The centre should help enhance the credibility of institutional arbitration in the eyes of the Indian judiciary and among arbitration users in India. In addition, LCIA India launched its own Arbitration Rules in April 2010. These rules incorporate various modifications to the original LCIA London Rules and several of these changes may be incorporated into the original rules when these are next revised.

Notable features of the Rules include:

- an easing of the threshold for accepting applications for interim measures;
- an increased emphasis on the obligation of parties to comply promptly with directions of the tribunal;
- an express requirement that prospective arbitrators confirm their ability to devote sufficient time to the conduct of the arbitration; and
- in cases where the parties have not specified the seat of the arbitration, a statement that India shall not be the "*default*" seat. The last of these provisions is a notable development, given the history of interference by the Indian courts in arbitration.

To use the Rules, parties must insert an appropriate clause to this effect in their arbitration provisions. A model clause to achieve this is set out in the Rules.

FINAL THOUGHTS

Despite its shortcomings, arbitration still occupies a prime position in commercial dispute resolution in India. However, it is still evolving, and has not yet matured to the extent required to keep up with the growth of investment in India. There have been a number of significant interventionist judgments, and although Indian courts do try to avoid interfering with the arbitral process, it is plain that there are still inherent problems to which corporations should be alive.

The good news is that the introduction of LCIA India and the potential changes to the 1996 Act are encouraging signs of progress for the Indian arbitration environment. Their success will hopefully assist in establishing the effective, expeditious and confidence-inspiring dispute resolution framework to which India aspires.

Raid Abu-Manneh
RAbu-Manneh@mayerbrown.com

Rebecca Downing
RDowning@mayerbrown.com

Construction & Engineering Group (UK)

ARBITRATION IN THE MIDDLE EAST - THE UPDATED QUICK REFERENCE GUIDE

Our Middle East team has updated their quick reference guide to key facts on international arbitration in the Arab countries of the Middle East.

Remind me - which countries does it cover?

Algeria, Bahrain, Egypt, Iraq, Jordan, Kuwait, Lebanon, Libya, Morocco, Oman, Qatar, Saudi Arabia, Syria, Tunisia, UAE and Yemen.

And what information does it provide?

- **New York Convention**: Has a country acceded to the New York Convention? If so, on what basis and when?
- **ICSID Convention**: Has a country acceded - and when?
- **Inter-Arab conventions**: Is a country signatory to any of the Arab conventions relevant to arbitration - the Riyadh and the GCC Conventions?
- **Local arbitration law**: What is the arbitration law of each country? When was it enacted?
- **Local arbitral institutions**: Does a country have a local arbitration institution and (if figures are available) how many cases is that institution presently administering?
- **Bilateral investment treaties**: what bilateral investment treaties has each country entered into?
- **ICSID Cases**: the number of pending and concluded cases.

If you would like a copy of the new edition please contact:

Raid Abu-Manneh
RAbu-Manneh@mayerbrown.com
+44 20 3130 3773

or

Wisam Sirhan
WSirhan@mayerbrown.com
+44 20 3130 3028

ARBITRATION IN INDIA – A NEW GUIDE

Our arbitration team has also produced a guide to arbitration in India. The guide summarises key information on Indian arbitral bodies, arbitration rules, the role of the Indian courts, rights of appeal and enforcement issues and offers practical guidance on avoiding pitfalls in arbitrating in India.

What does the guide cover?

- the applicable arbitration rules, identifying the mandatory provisions;
- the Conventions to which India is signatory;
- the principal arbitration institutions;
- the supervisory powers of the national courts;
- the validity of an arbitration agreement under Indian law;
- the nomination and removal of arbitrators, procedure and evidence;
- interim measures;
- rights of appeal;
- the applicability of the New York Convention; and
- costs.

If you would like a copy please contact:

Raid Abu-Manneh
rabu-manneh@mayerbrown.com
+44 20 3130 3773

or

Rebecca Downing
RDowning@mayerbrown.com
+44 20 3130 3183

Don't go OTT in your NDA for an ITT

NDAs are usually a good thing. We often recommend to clients in the construction industry that they should do what is common in other sectors and ensure that, before they disclose proprietary information, they get the recipient to sign up to a non-disclosure agreement (NDA, for short, also called a confidentiality agreement). As we see in the ***Veolia*** case (see page 25), things are not always straightforward, but getting an NDA is usually a good starting point. There are, however, legal downsides if you try and go too far in the restrictions imposed in the NDA, as shown in a case last year, ***Jones v. Ricoh***.

A company called CMP had been in business helping customers to save money on photocopiers, scanners etc. It charged end users on the basis of the savings it obtained for them. Over the years, it built up a relationship with Ricoh and CMP's customers bought directly from Ricoh, which became the main supplier that CMP dealt with. CMP's main customer was rail systems company ADtranz, which was later acquired by the Canadian group Bombardier. CMP was worried that it might get cut out of the relationship between Ricoh and the users of the photocopiers, so it entered into an NDA with Ricoh. The problem was that the NDA went beyond the normal terms of restricting Ricoh's use of confidential information about CMP's terms and customers. Indeed, one of its provisions prohibited not just Ricoh but any associated company (of which there were 150 around the world) making any approach or contact with any employee, client or supplier of CMP – or any government body or regulatory authority – for so long as Ricoh had CMP confidential information in its

possession. The judge described this clause as "extraordinarily wide". In particular, the prohibition was not limited to those who had been customers of CMP while it dealt with Ricoh, nor to customers in respect of whom Ricoh had relevant confidential information of CMP's. The period of time covered by the restriction was indefinite in practice, since it lasted for so long as Ricoh had any of the proprietary information. It would even have prevented Ricoh dealing with pre-existing customers who were nothing to do with its relationship with CMP.

Bombardier issued an invitation to tender for the supply of photocopiers etc., and, to CMP's surprise, Ricoh bid separately rather than putting in a joint bid with CMP. CMP put in a bid with Toshiba and they won, but later lost the Bombardier business because the machines were incompatible. Another ITT went out and this time Ricoh won. CMP went into voluntary liquidation and its MD, Mr Jones, sued Ricoh for breach of the NDA. The amounts claimed ranged between £4 million and £49 million.

Ricoh retaliated by saying that the broadly drawn NDA was in breach of competition law (and more specifically Article 101 of the EU treaty which prohibits anti-competitive agreements, i.e. agreements which have as their object or effect the prevention, restriction or distortion of competition within the EU). So the case is interesting in its application of EU competition law to the subject of confidentiality agreements, which are not often looked at by the courts in this context.

The judge felt that it was clear that the NDA went "*very far beyond any possible view of what could be needed*" for the purpose of protecting CMP's confidential information. It was a "*naked restriction on any of the more than 150 Ricoh companies dealing with or seeking to deal with a client of CMP*" and although NDAs do not normally qualify as agreements which are regarded as anti-competitive by object, this one did. CMP tried to defeat the competition law attack by referring to one of the block exemptions which exempt certain types of agreements from competition law, but the "*vertical agreements*" block exemption did not help, because CMP did not buy photocopiers for resale but rather helped its customers to buy them direct from Ricoh.

So the offending clause was shot down as being void and unenforceable under EU competition law. The part of the case relating to this clause was so clear that Ricoh succeeded in getting summary judgment i.e. having that element of the claim struck out. (The case continued in relation to Mr Jones' claim that Ricoh should not have responded to the ITT on its own, rather than as a joint bid with CMP.)

The lesson from ***Ricoh*** is therefore that any provisions in an NDA going beyond the protection of confidential information need to be looked at carefully from a competition law point of view. Going OTT can deliver the KO to an NDA.

Sarah Byrt
SByrt@mayerbrown.com
Intellectual Property and Information Technology Group

Competition Appeal Tribunal slashes OFT cover pricing fines

The UK's Competition Appeal Tribunal has reduced to a fraction of the original amount the fines imposed by the UK Office of Fair Trading on six construction companies in the construction cover pricing case. The CAT's judgment, handed down on 11 March 2011, criticises the OFT's view of the seriousness of the infringements concerned and the OFT's "one size fits all" approach to adding a deterrence factor to the companies' basic fines.

The judgment will be a significant blow to the OFT, as it has reduced fines totalling £41.78 million to £4.4 million. It is likely to force the OFT to reconsider its approach to calculating penalties in future cases.

The six companies are among the 25 companies that appealed the OFT's September 2009 decision to impose heavy penalties on 103 construction companies it found had engaged in cover pricing between 2000 and 2004. Judgment in the remaining 19 appeals is still awaited.

The CAT's composite judgment upholds appeals by Kier, Ballast, Bowmer, Corringway, Thomas Vale and Sisk. Kier's original fine was the largest imposed by the OFT, at £17.9 million – this has been reduced by nearly 90%, to £1.7 million. The largest reduction, of 94.2%, was awarded to Sisk, whose £6.2 million fine - for one single infringement - the CAT has reduced to £356,250.

The key factors in the CAT's judgment, and their implications for the future, are as follows.

- **The level of seriousness attributable to cover pricing was too high**

The OFT calculates the basic fine by applying a percentage figure to the infringer's turnover in the market affected by the infringement. This figure can be 0-10%, depending on the seriousness of the infringement. The CAT has commented that this range may be too narrow and has invited the OFT to reconsider it when revising its 2004 guidance on penalties.

The CAT has reduced the OFT's 5% to 3.5%, for two main reasons:

- **The nature of cover pricing:** Although cover pricing was not innocuous, it did not merit the severity of treatment meted out by the OFT. The intentions of parties engaged in cover pricing are not to increase the price the customer should pay (as with normal cartel-type conduct), but to identify a price that the customer is not willing to pay, so that the firm receiving the cover price can be sure not to win the contract (a decision it has already made). Given that any tenderer wanting to win the contract will put forward its keenest bid irrespective of cover pricing, the harm caused is likely to be small compared with a hardcore cartel.
- **Industry practices at the time of the infringements:** During the period 2000 to 2004, when most of the infringements took place, the perception in the industry was that cover pricing was acceptable.

Although it did not affect the outcome of the appeals, the CAT also criticises the OFT's narrow approach to defining the markets affected by the various infringements

– the turnover used to calculate the basic fines varied significantly among the 120 markets the OFT identified, resulting in widely different basic fines for the same conduct. This is likely to have an impact on the OFT's future approach – it may adopt a wider definition of the relevant market in similar circumstances in future.

- **The turnover used in calculating fines should have been turnover from the year preceding the infringement**

The CAT criticises the OFT for departing without proper consultation from its pre-2004 practice of calculating fines on the basis of turnover in the year before the infringement. It finds that the OFT's 2004 penalty guidelines do not make it clear that the OFT has switched to using turnover in the year prior to its infringement decision, and it finds that this was not highlighted in the OFT's consultation on the draft guidance. The OFT was not entitled to say that the statutory change in the basis for calculating the maximum fine justified its change in approach at earlier stages of calculating the fine, since the statutory change related to the affordability of the fine and not punishment and deterrence.

Until the OFT issues specific guidance, therefore, it appears that the turnover it must use in future cases is turnover in the year preceding the year of the infringement. This may make a significant difference to a company's basic fine.

The CAT also criticises the OFT's approach to calculating the penalty for Ballast. Ballast's turnover in the year preceding the decision had been zero, as it had withdrawn from the UK market. The OFT adopted a proxy of 0.14% of Ballast's global turnover as the basis for its calculation, taking the median of the step 2 penalties for all infringers, expressed as a percentage of worldwide turnover. The CAT finds that this produced an unfair result for a company that had less than 1% of its turnover in the UK. Although the CAT's discussion was academic (Ballast had generated turnover in the relevant market in the year preceding the infringement and so no proxy was required for the CAT's calculation of its penalty), and a proxy may be relevant only in rare circumstances, the OFT has a clear message that its approach needs to ensure fairness and take account of the infringer's specific circumstances.

- **The OFT's blanket approach to increasing the basic fines for deterrence was wrong**

The most significant factor in the reductions in the six companies' fines is the CAT's rejection of the OFT's approach to increasing basic fines for deterrence. This made a massive difference in the level of fines, frequently increasing them by several hundred fold.

The OFT has discretion to add a deterrence factor to a basic fine it considers is insufficient to deter the infringer and companies more generally from similar practices in future. The OFT's approach has been to apply the percentage seriousness figure to 15% of the turnover of the infringer's global group ("the MDT formula"), instead of applying it to the infringer's turnover in the market affected by the infringement. The deterrence factor is the difference between the two calculations.

The CAT says that there is nothing inherently objectionable in the OFT's approach, but that the MDT is not a substitute for individual assessment of each case: the MDT

should not be allowed to result in the imposition of a final penalty that is excessive and disproportionate

The CAT criticises the OFT's mechanistic, blanket approach:

- The OFT applied the same formula to all companies without standing back and assessing the impact in individual cases, to confirm that in all the circumstances a penalty at the proposed level was reasonable and proportionate to punish the infringer and deter it and other companies from further similar breaches.
- The choice of 15% of the infringer's global group turnover as a basis for the deterrence factor was not explained and was a "blunt instrument".
- The OFT did not look at factors other than turnover, such as profits and cashflow – it noted the low margins in the construction industry and the fact that revenues often incorporated invoiced amounts for sub-contractor work.
- Proportionality requires a balance between the culpability of the infringer and deterrence. The OFT did not ensure this balance. It is entitled to upscale the penalty for deterrence, but "culpability must not be lost to view".

The judgment is likely to bring about a significant change in the OFT's fining practices – it will clearly need to consider a tailored approach to deterrence in individual cases. The fact that the CAT queries the OFT's choice of 15% global group turnover as the basis of the MDT formula, describing it as a "blunt instrument", must compel the OFT to give careful consideration to its continued use. The question is what, if anything, should take its place. It is interesting not only that the deterrence factors added by the CAT in each case were very substantially smaller than the deterrence factors applied by the OFT, but also that the CAT does not appear to have used any formula of its own in arriving at the appropriate figure.

- **Discounts for compliance measures are acceptable**

The CAT indicates that post-infringement compliance programmes should be taken into account in assessing the deterrence factor, as they have a bearing on specific deterrence. The OFT has been reluctant to do this in the past, so it will be interesting to see how it applies this in the future.

The CAT also states that it does not dispute the OFT's practice of awarding some mitigation discount for a post-infringement compliance programme, since this induces infringers to take appropriate steps to avoid infringing in the future. However, it indicates that, although the size of the discount will depend on the specific circumstances of the case, in most cases it is likely to be relatively modest in relation to the overall fine. In the majority of cases, the discount awarded by the OFT was 5%.

- **Fraud by an employee does not negate or reduce the need for punishment or deterrence**

One of the six appellants, Bowmer, was found to have made a compensation payment to another bidder in relation to a tender Bowmer had won. The compensation payment had been arranged by a Bowmer employee without Bowmer's knowledge or consent. Since this was not a case of simple cover pricing, the company's penalty was

higher – the OFT's starting point percentage was 7% rather than 5%. The CAT rejected Bowmer's argument that the penalty should be reduced on the basis that the company was the victim of fraud – the CAT said that the employee concerned had acted in Bowmer's interests. The CAT applied the 7% starting point to calculate the basic fine and then doubled the fine for deterrence.

The OFT has a month from the date of the judgment in which to appeal to the Court of Appeal, on a point of law – and it must obtain permission either from the CAT or from the Court of Appeal before it can do so. In the meantime, the CAT's judgment makes it likely that the OFT will consider changes to its 2004 guidance, to include:

- broadening the range of starting point percentages,
- clarifying the turnover to be used in calculating penalties and
- further guidance on the calculation of the deterrence factor.

It is also likely to consider changes to its practices, including a broader approach to defining the markets affected by the various infringements and a more tailored, proportionate approach to deterrence, balancing it against culpability in the case of each infringer.

Gillian Sproul
gsproul@mayerbrown.com
Head of Antitrust and Competition Group (London)

Extras

The amended Construction Act – when does it start?

The latest (unofficial) word on the start date for the amended Construction Act to come into force is that the target is 1 October 2011.

The amended Act will apply to contracts entered into on or after a specified date. This raises the challenging possibility, on projects then in progress, of some subcontracts being governed by the unamended Act and others (including oral contracts) by the amended Act. The same issue may arise in connection with framework agreements, if each new order is a contract rather than an instruction. The framework agreement may also not cater for the new payment machinery introduced by the amending Act.

And once a date is set there will then be the not insignificant matter of amendments to the standard contract forms, notably JCT and NEC3.

COMMUNITY INFRASTRUCTURE LEVY TO CONTINUE – WITH CHANGES

The Government is to retain the Community Infrastructure Levy but it is to be reformed to ensure neighbourhoods receive a proportion of the funds councils raise from developers so that community groups can spend the money locally on the facilities they want. The new system will be more transparent, with levy rates set in consultation with local communities and developers, who will know in advance exactly how much they will be expected to pay towards infrastructure. Some changes to the CIL require

amendments to legislation and regulations but no significant changes will be made to Section 106 agreements.

See: http://www.communities.gov.uk/news/corporate/176860911

LOCALISM BILL – POWER TO THE PEOPLE?

The Localism Bill laid before Parliament shortly before Christmas contained a number of proposed reforms intended to give greater power and freedoms to councils and neighbourhoods and to change the planning system. Included in the package is the removal of Regional Strategies. The Government's first attempt to revoke the Strategies resulted in a successful challenge in the High Court by Cala Homes, and the Government's subsequent further advice to Chief Planning Officers was met by further proceedings launched by Cala, that, this time, were unsuccessful (subject to appeal).

Also included in the Bill is a requirement for prospective developers of very large developments to consult local communities before submitting planning applications. Developers will have to have regard to any opinions raised during this consultation when deciding whether to make any changes before submitting their planning applications.

See: http://www.communities.gov.uk/documents/newsroom/word/1795339.doc

AND THE FUTURE IS …40 YEARS OF CONSTRUCTION WORK…BUT…

The good news, from the final report of the Innovation and Growth Team, is that, over the next 40 years, the transition to low carbon can almost be read as a business plan for construction. The catch is that, to meet the commitments of the Climate Change Act, there are a number of barriers to be overcome, and probably, according to IGT, the biggest change management programme that the construction industry and society has faced since Victorian times. The IGT has identified what is needed, including reform of the industry and its working practices; the IGT consensus is that it is scarcely possible that the innovation and change essential to deliver effective and affordable low carbon solutions can be secured through the industry as currently structured and engaged, particularly in the lack of collaborative integration of the supply chain, and in the "silo-based" habits of the industry's institutions. If the various barriers to progress can be overcome, however, the IGT sees five great opportunities, including a "*huge programme of work, stretching out over at least the next 40 years*".

See: http://www.bis.gov.uk/constructionigt

AND A SHAKE UP FOR BUILDING STANDARDS

The Government is scrapping proposals for new Core Standards for development that is funded, or on land owned by, the Homes and Communities Agency, which could, on average, have cost developers an additional £8,000 per home. The Government says that, in the long term, the standards that apply to private and public housing should be the same.

Work is to start on a new Local Standards Framework to be developed and maintained by industry and councils (with the Government's help). The new

framework will be implemented through the National Planning Policy Framework, to be introduced by April 2012. The Government has also confirmed that the recent review of the Building Regulations will be published shortly, and will keep the regulations as the mechanism to set national minimum standards. Developers now have the opportunity to make suggestions for further deregulation of the industry.

See: http://www.communities.gov.uk/news/planningandbuilding/1779916

EU PROCUREMENT RULES – UNDER REVIEW

The European Commission is undertaking a comprehensive evaluation of the EU public procurement rules and the Cabinet Office has sought feedback on the effectiveness of the rules. It will use the feedback to influence the Commission's evaluation and any proposals for change. While the scope of the Commission's review is broad, the amended standstill and remedies rules are excluded. The Commission aims to make proposals to simplify and update the rules in 2012 at the latest.

The Cabinet Office identified a number of rule provisions that it considers likely to be in need of modernisation: raising the thresholds, simplifying the competitive dialogue procedure, improving framework agreements, simplifying the dynamic purchasing systems rules, reducing minimum timescales, improving the selection process through standardised qualification, transparency of suppliers' past performance and clarity on considering and evaluating wider policy agendas in procurement decisions.

AGGREGATES GO INTO THE COMPETITION MIX

In September 2010 the OFT launched a market study into the UK aggregates sector which, in 2008, had a turnover of 4.8bn. The study is looking at the high barriers to entry in the sector, increasing concentration at local level and Government involvement in a national system of control over outputs, to determine how these factors influence competitive conditions and whether the market delivers good value for money to taxpayers and end consumers, as the cost flows through to the construction of essential infrastructure. The study is expected to be completed by July 2011.

JACKSON COSTS PILOT

Lord Justice Jackson's costs management initiative, presently the subject of a pilot in the Birmingham Mercantile Court, is to be extended to every Technology and Construction Court in October. Judges are to have costs management training in May. A bill to implement the Jackson reform proposals that the Government wishes to take forward is said to be "highly likely" by July.

GOVERNMENT TARGETS 2019 FOR ZERO CARBON COMMERCIAL BUILDINGS

Grant Shapps, Minister for Housing and Local Government, has confirmed that Government policy is progressively to raise the national regulatory requirements for non-domestic buildings between now and 2019, enabling them to be "zero carbon" from 2019. Consistency between the domestic and non-domestic frameworks (with the target date for new build homes being 2016) is to be maintained as far as

practical, but a different approach may be taken on some elements, where justified by the diversity of the non-domestic stock or the nature of the commercial market. A figure of £500 billion has been suggested as the possible cost of compliance for commercial property owners.

STANDARD CONSTRUCTION DOCUMENTATION IN CHINA

China has been developing standard documents for construction projects since the early 1990s and has published further draft construction documents for public consultation. For an update on the latest documents by Geoffrey Chan (geoffrey.chan@mayerbrownjsm.com) in our Hong Kong office and Tom Fu (tom.fu@mayerbrownjsm.com) in our Beijing office, see: http://www.mayerbrown.com/publications/article.asp?id=10500&nid=6

1 OCTOBER 2011: DID YOU KNOW ABOUT THE NEW LAW ON AGENCY WORKERS?

The Agency Workers Regulations 2010, which come into force in the UK on 1 October 2011, say that the basic working and employment conditions of temporary agency workers must be the same as individuals recruited directly for the job. Although agency workers will have limited rights from day 1 of an assignment, the main feature of the Regulations is the requirement that agency workers will be entitled to the same basic working and employment conditions as if they had been recruited directly by the hirer, once they have completed a 12 week qualifying period. For a copy of our Guidance Note, please call or email Chris Fisher (CFisher@mayerbrown.com +44 20 3130 3724).

HOW TO FIND GOVERNMENT CONTRACT OPPORTUNITIES

Following the government's start on publishing, in full, every central government contract over £25,000, it has launched an online tool to display every central government tender opportunity, with an email alert facility to advise prospective tenderers when new opportunities in their area of business arise. (See: http://www.contractsfinder.businesslink.gov.uk/). The government is also looking to eliminate the prequalification process for lower-value procurements and is announcing a series of surgeries where companies with innovative products and services can come and pitch to government – rather than waiting for the right tender to be issued.

NSCC IN WAR ON RETENTION

The National Specialist Contractors Council has adopted a no retention policy and is recommending that, while its specialist contractors are free to negotiate their own contract terms, at the outset of a project, the specialist subcontractor should inform the contractor or client that they do not accept cash retention and propose a retention bond as an alternative. If the contractor will not negotiate, the NSCC advises considering offering a discount (e.g. the retention value) in return for no cash retention or a reduced retention rate for the last few payments. If neither of these is accepted, the NSCC tells its members to decide if they are prepared to work for that contractor or client. The NSCC website provides advice and draft letters to underpin the campaign. It has since been reported that Crossrail will not be holding cash retention on any of its contracts but will instead be looking for a 2.5% retention bond from the main contractor. For further details see: http://www.fairpaymentcampaign.co.uk/removal-of-retentions.asp

Consultant passes Sandwich supermarket test

In the late 1990s the Co-op in Sandwich was possibly not a safe place to park a trolley. Its floor slab, resting partly on improved ground and partly on the superstructure pile caps, suffered differential settlement of up to 110mm – enough, perhaps, to set even a sluggish trolley in motion. The problem was that the ground under the slab was not improved enough, and for that the Co-op blamed the structural engineers who had produced the soil stabilisation performance specification. Armed with a desk study report from the original employer's geotechnical and environmental consultants, which assessed the likely ground conditions and calculated the extent of long term settlement, the engineers had relied on advice they had obtained from a specialist subcontractor. But were they entitled to do that?

In ***Cooperative Group Ltd v John Allen Associates Ltd*** the Co-op claimed that the engineers could not delegate their design liability in this way. Among other cases, they referred to the classic 1966 decision in ***Moresk Cleaners Limited v Hicks*** where the court said that an architect could not escape responsibility for their design by delegating their work. But was that really what JAA had done?

Mr Justice Ramsey said it was not. It was not a question of whether the engineers had delegated their duty to a third party but whether they had acted with reasonable skill and care in seeking and relying on advice from a specialist subcontractor instead of carrying out their own evaluation or obtaining independent advice. He analysed the case law, including ***Moresk,*** and came up with three propositions, that:

- construction professionals do not by the mere act of obtaining advice or a design from another party thereby divest themselves of their duties in respect of that advice or design;
- construction professionals can discharge their duty to take reasonable care by relying on the advice or design of a specialist, provided that they act reasonably in doing so;
- in determining whether construction professionals act reasonably in seeking the assistance of specialists to discharge their duty to the client, the court has to consider all the circumstances, which include:

  (a) whether the assistance is taken from an appropriate specialist;

  (b) whether it was reasonable to seek assistance from other professionals, research or other associations or other sources;

  (c) whether there was information which should have led the professional to give a warning;

  (d) whether and to what extent the client might have a remedy in respect of the advice from the other specialist; and

  (e) whether the construction professional should have advised the client to seek advice elsewhere or should themselves have taken professional advice under a separate retainer.

He decided, on the evidence, that the engineers had acted reasonably in seeking and relying on advice from the specialist subcontractor and did not themselves need to carry out an evaluation to confirm or criticise the advice or seek an evaluation from another consultant engineer. And even if the advice of the specialist subcontractor had been negligent, they would still *not* have been in breach of their duty of care.

AND THE STANDARD OF CARE IS?

The judge also confirmed that the standard against which to benchmark the engineers' performance was that of an ordinarily competent structural and civil engineer, exercising ordinary care and skill, and assessing their conduct against the terms of the warranty given to the Co-op. The standard is that of *"the reasonable average"* and the court has to be careful to judge the conduct by what was known at the time and not with the wisdom of hindsight.

The Co-op had called a leading geotechnical engineer as expert. Mr Justice Ramsey pointed out that, while that expert could provide useful evidence, he, the judge, had to be cautious not to attribute to the structural engineers a duty to act as a professional geotechnical engineer would have acted in the circumstances of the case.

CAUSATION

Mr Justice Ramsey also considered causation and the appropriate measure of damages in a claim against a construction professional for negligent design.

The first stage, he said, was to establish what would have happened if the construction professional had exercised proper care and skill. If the claimant could show that, if the professional had used proper care and skill, the claimant would have proceeded with the construction of the building in accordance with the proper design, then the measure of damages would be the cost of remedying the defect, less a credit for any higher costs that would have been payable for a proper design in the first place.

If, however, the claimant would have abandoned the project if the professional had produced a properly prepared design, then the recoverable loss would be measured by reference to the wasted expenditure.

THE FUTURE

Once remedial works are carried out, the shoppers of Sandwich should be able to look forward to a future in which their trolleys will no longer be rolling in the aisles.

Richard Craven
RCraven@mayerbrown.com

Construction & Engineering Group (UK)

How substitutions can change the employment game plan

The employment status of individuals working in the construction industry often comes before the employment courts. The question is frequently whether the individual is self-employed or a "worker", someone who is not an employee but does perform work personally for a third party. The distinction is important because, unlike the self-employed, workers are entitled to certain legal rights such as statutory holiday and minimum wage.

The individual's contract will often contain a "substitution" clause, which allows them to provide someone else to perform the work. The argument runs that, if the substitution clause is genuine and unqualified, then there is no obligation of personal service and the individual cannot be a worker. The courts, though, are quick to scrutinise the use of such clauses. If the right to provide a substitute is limited in some way, there may still be a finding of worker status. For example, where the substitution right exists only if the individual is unable (as opposed to unwilling) to carry out the work himself.

A recent case involved a dentist but will set a precedent which will be applied across all industries. His contract said he was self-employed but he claimed he was in fact a "worker". The dental centre where he worked argued that he could not be a worker because his contract contained a substitution clause which provided that, instead of working himself, the dentist could arrange for a locum to take his place.

The dentist claimed that the obligation to arrange a locum was in itself a personal service sufficient to maintain his status as a worker, but the court disagreed. The substitution clause was unqualified: it could apply whether the dentist was unable or simply unwilling to work himself. This, said the court, was fatal to his claim to be a worker because it meant there was no obligation of personal service. The fact that he was required to arrange a locum substitute did not detract from the fact that he himself was not obliged to perform the work personally.

A carefully drafted substitution clause can therefore limit an individual's ability to claim worker status, but be careful. A substitution clause must be genuine: the parties must intend it to be used in practice. If it is a sham, the court will ignore it and may still make a finding that the individual is a worker – with all that that entails.

Christopher Fisher
CFisher@mayerbrown.com
Employment Group

This article first appeared in a slightly different form in *Construction News*.

Has time been called on corporate hospitality?

Corporate hospitality, Wimbledon, lunches and all the rest are what might be called an accepted part of commercial life. Bribery? Surely not? But, from this April, the radically modernised anti-corruption legislation in the new Bribery Act was scheduled to place a significant question mark over corporate hospitality*.

The new Act will apply to those doing business in Britain and UK companies and residents doing business abroad. Not only individuals will be open to criminal prosecution; companies may be liable for failing to implement adequate measures to prevent their employees and agents paying bribes to win business.

The new Act's main offences are very broad and based around the idea of a bribe being an inducement or reward for someone performing their job improperly. A bribe is not limited to the classic brown envelope stuffed with banknotes, but means any type of "advantage" whether it has direct monetary value or not. It can therefore include gifts, corporate hospitality, donations, favours or even providing information. Even trivial gifts may potentially be caught by the legislation where the "improper" test is met.

An offence can also be committed by a recipient of an "advantage", where acceptance in itself constitutes improper performance of their job, and by the person offering the "advantage", if they know that; for example, where an organisation has expressly prohibited its employees from accepting gifts from its suppliers.

On its face, therefore, excessive corporate hospitality could expose the host and recipient to criminal prosecution. Suppose a host offers high value entertainment (e.g. an all expenses paid trip to the World Cup), knowing or believing that acceptance would breach internal policies of the recipient's organisation; that could be a bribery offence. Similarly, if the person to be entertained "requests, agrees to receive or accepts" this high value hospitality and this infringes their organisation's internal rules and policies, they are also at risk of prosecution.

Which means it is now vital that all commercial organisations have an effective policy on the giving and receiving of gifts and corporate hospitality and that their employees and other representatives are fully aware of that policy. This is not only to reduce the risk of prosecution of those individuals, but also to ensure the organisation itself is not exposed to criminal liability and potential reputational damage.

Andrew Legg
alegg@mayerbrown.com

Susan Rosser
srosser@mayerbrown.com

Litigation and Dispute Resolution Group

This article first appeared in a slightly different form in *Construction News*.

*Since this article was prepared the coming into force of the 2010 Bribery Act has been postponed - to 1 July 2011 and, as this Update was going to press, the Government guidance was published.

PFI and procurement review

IS PFI AN ENDANGERED SPECIES?

Before last year's election George Osborne said that the Conservatives would scrap the Private Finance Initiative and replace it with an alternative model for large infrastructure projects. *"Labour's PFI model is flawed and must be replaced"*. So did the October Comprehensive Spending Review include PFI among its intended victims?

Traditionally, infrastructure was procured conventionally, with the capital cost being funded by central or local government but more recently Public Private Partnerships have taken centre stage. PPP involves risk sharing between the public and the private sectors and has encompassed concessions, joint ventures and Strategic Infrastructure Partnerships (most notably Building Schools for the Future) but its most famous member is PFI.

Originally introduced in 1992 by Chancellor Norman Lamont, PFI has mushroomed over the last 10 years under New Labour. At the last count, there were 920 PFI projects that had achieved financial close at a total value in excess of £70 billion.

The arguments for and against PFI are well rehearsed, but one particular aspect, the accounting treatment, looks attractive in these times of austerity. When capital budgets are being squeezed, PFI provides an alternative way of procuring large infrastructure without the government having to provide the capital up front or declare the corresponding debt (as PFI debts are treated as off-balance sheet).

Despite that (and perhaps unsurprisingly in the light of George Osborne's comments), PFI seems to be falling out of favour with the coalition government. Election night saw Tube Lines Limited, the last remaining PPP contractor on the London Underground following Metronet's collapse, taken back in house. The BSF programme for schemes that had not reached financial close plus 39 road programmes worth £1.6 billion were scrapped and other projects that had not reached financial close were put in limbo awaiting the outcome of the CSR. So is it goodbye to PFI then?

The CSR axe fell less hard than expected and infrastructure fared much better than other areas, with the biggest winners being transport and education. On the other hand, PPP as a procurement method has not done so well, particularly in education with the Chancellor's CSR speech referring to the cancelled BSF programme as "*hopelessly inefficient and over-committed*".

However, the Department for Transport confirmed a number of local authority PFI schemes (including the extension to the Nottingham Express Transit Tram network) and, according to the DfT, local PFI spending is to increase by 71% over four years. Which left us with mixed messages – a cancelled BSF programme but increased PFI spending on local transport, while at the same time suspending further lending by the Infrastructure Finance Unit. And wondering where exactly we are headed on infrastructure and, for that matter, PFI.

Raid Abu-Manneh
RAbu-Manneh@mayerbrown.com

Wisam Sirhan
WSirhan@mayerbrown.com

Construction & Engineering Group (UK)

POSTSCRIPT

This article first appeared in a slightly different form in *Construction News*. Since then the House of Commons Treasury Committee has announced an inquiry and a call for evidence on the future of PFI and the Treasury Plan for Growth, published with the March Budget, has promised the Government will publish the UK's long term forward view of projects and programmes in the autumn as part of the National Infrastructure Plan 2011. From the autumn the Government is also to publish a rolling two year forward programme of infrastructure and construction projects, where public funding has been agreed.

The Plan for Growth also says that the Government will reform the way in which it procures public sector construction and infrastructure to reduce costs by up to 20 per cent. This will include measures to encourage standardisation rather than bespoke designs, setting clear criteria for asset performance and introducing new models of procurement. A detailed programme of measures to achieve this will be published before the end of May 2011.

AND IS THERE AN ALTERNATIVE?

In the week following the October 2010 spending review, Infrastructure UK (the part of the Treasury responsible for PPP/PFI) produced the *National Infrastructure Plan which, in the words of the Chancellor, would set out how "*private money is also put to work in building for this country the economic infrastructure our businesses need*".

The 2010 Plan focuses on "*economic infrastructure*", a term that includes the energy, transport, digital communications, flood protection and water and waste management sectors. So does The Plan deliver on the Chancellor's promise and where, if anywhere, does it leave the Private Finance Initiative?

The Plan outlines the general direction of infrastructure investment, identifies the key forthcoming consultations and reports to be added to it and is to be reviewed regularly, with an update scheduled for the end of 2011. It is, however, remarkably light on references to PPP/PFI, with only one reference to PFI in the main body of the Plan, and that in relation to projects already completed or in procurement. So if PFI is facing extinction, what exactly is going to replace it?

Tax Increment Financing

Despite the scary title, this could be an attractive way to get private money and investment into infrastructure. In plain English, TIF allows local authorities to borrow capital sums (for infrastructure or other key developments) against predicted future growth in locally raised business rates. Although it may be new to the UK, TIF has been widely used in the United States of America to fund infrastructure and redevelopment schemes for over half a century.

Currently, all locally raised business rates flow back to the Treasury, and a change to allow these to be retained locally would be a radical departure from the way in which local government finance currently operates. Significant legislation would be required to achieve this, but the wheels have already been set in motion and TIF was promoted in the October Local Government White Paper on local growth.

* and see also the 2011 Treasury Plan for Growth, above.

And a real live TIF project may not be that far away. Wandsworth Council, which is in part responsible for the redevelopment of Nine Elms and the iconic Battersea Power Station, has indicated that it is examining the potential for TIF to provide at least some of the funding for the Northern Line Extension (currently costed at around £560 million) that will be part of the redevelopment.

Regulatory Asset Base

But the solution that emerges from The Plan is Regulated Private Ownership, a preferred method of attracting private investment in public infrastructure, which will be familiar to those involved in the water and electricity sectors, as well as other regulated monopolies created by privatisation. To take this approach forward, the Regulated Asset Base model seems to have emerged as a favourite. In a nutshell, the RAB model is a regulatory mechanism for recovery of costs sunk into major capital investment. The mechanism sets a rate of return for investors as well as regulating outputs for the end users, in an attempt to strike a balance between return and utility.

According to The Plan, the stability and certainty of a regulatory regime encourages private investment, with the additional benefits of reducing the cost of capital (one criticism of PFI) and therefore the overall cost of procurement. This looks like a way of encouraging private investment at a lower cost, but is it really alchemy, and too good to be true?

The Plan acknowledges weaknesses in the RAB model, including the transfer of certain risks to consumers and questions as to affordability and whether this risk transfer would put too great a burden on certain members of this group. To address these issues, the Government is to carry out an internal review, with input from external experts, to consider extending the use of the RAB model. The review report is due this Spring.

But whatever the outcome of the review and whether or not TIF or RAB is the new, younger, model that will take the place of PFI, the Plan has done nothing to challenge the Chancellor's comment of last year, that *"Labour's PFI model is flawed and must be replaced"*. It will be interesting to see if the House of Commons Treasury Committee inquiry comes to a similar conclusion and what the Chancellor's "*new models of procurement*" might be.

Raid Abu-Manneh
RAbu-Manneh@mayerbrown.com

Wisam Sirhan
WSirhan@mayerbrown.com

Construction & Engineering Group (UK)

WHY PFI CONTRACTORS SHOULD BE GRATEFUL FOR HUMAN RIGHTS LAW

Commercial confidentiality is rather important. So important that the freedom of information legislation provides confidentiality with exemptions but, for PFI contracts, it looked for a while as if Mr Justice Cranston had unearthed a way round that protection. Until, that is, the Court of Appeal intervened, with the help of EU human rights law.

When a Nottinghamshire elector opposing a proposed incinerator failed, under the freedom of information legislation, to obtain key financial documents relating to a PFI waste management contract awarded by Nottinghamshire County Council to Veolia, he turned to the courts. Mr Justice Cranston decided that the documents had

to be disclosed to "*any persons interested*", because s15(1) of the Audit Commission Act 1998 gave such persons rights to inspect documents "*relating to*" the Council's "*accounts to be audited*" and the documents in question were information "*relating to*" the accounts. Ominously for PFI contractors, the judge also decided that commercial confidentiality was no bar to disclosure.

The Court of Appeal agreed that the documents were information "*relating to*" the accounts but, on appeal, Veolia had added two new arguments. It said that the s15(1) right of inspection did not extend to confidential information and that the use to which information provided might be put should be limited.

The Court agreed with Veolia that section 15(1) should be read down so as to exclude confidential information. Case law of the European Court of Justice and the European Court of Human Rights supported the proposition that the use of confidential information in professional or commercial activities *of even legal persons* could be protected as an element of their "*private life*", under Article 8 of the European Convention on Human Rights, subject to disclosure justified in the public interest.

Article 1 of the Convention's first protocol also says that every natural *or legal* person is entitled to the peaceful enjoyment of his possessions and that no one is to be deprived of them except in the public interest and subject to the law's conditions. In the absence of direct legal authority, Lord Justice Rix could see no reason why valuable commercial confidential information, such as the information in question in the case, could not be "*possessions*". At least Article 1 (and perhaps also Article 8) provided sufficient reason in the case to interpret S15(1) so as to make an exception for confidential information, subject to justified disclosure. Not to protect this information would, in fact, be potentially anti-competitive.

But should the use of disclosed information be limited? Lord Justice Rix was happy to decide the point but the other Lord Justices were not. On the basis of the confidentiality decision, however, it was suggested the point was unlikely to arise in the future.

PFI contractors may now breathe more easily about the confidential information in their tender bids, but public authorities face the potentially tricky challenge, when necessary, of balancing confidentiality against the public interest, for which the Court could not offer any clear-cut test.

Wisam Sirhan
WSirhan@mayerbrown.com

Richard Craven
RCraven@mayerbrown.com

Construction & Engineering Group (UK)
This article first appeared in a slightly different form in *Construction News*.

PROCUREMENT: HOW TO SPEND BILLIONS...

Hard on the heels of the Government's spending review came the Local Growth White Paper and the go-ahead for the first 24 local enterprise partnerships. Other proposals to promote local business growth include allowing local authorities to keep the local business rates they collect locally, a new system of Tax Increment Financing to enable local authorities to borrow against future increases in business rate revenues, a New Homes Bonus, starting in April, to match fund additional council tax raised for new homes for the following six years; a Renewable Energy Bonus, allowing local authorities to keep the business rates from renewable energy projects and the £1.4 billion Regional Growth Fund.

See: http://www.bis.gov.uk/assets/biscore/regional/docs/l/cm7961-local-growth-white-paper.pdf

The Government is also encouraging contract managers in central and local government to examine the potential for operational savings in PFI projects. Infrastructure UK has prepared draft guidance to assist the managers "*to identify and implement savings measures that will reduce costs while maintaining frontline services.*" A pilot project to identify the scope for achieving savings was launched in February. It will involve an experienced team of commercial, legal and technical advisers identifying ways of reducing ongoing costs under the contract for the Queen's Hospital in Romford. Amended guidance will be issued following the conclusion of the pilot.

IUK is also pursuing a voluntary Code of Conduct with investors, subcontractors and lenders at a national level. The purpose of the code is to address, in principle, operational savings matters that are likely to be generic across projects.

See: http://www.hm-treasury.gov.uk/d/iuk_making_savings.pdf

...AND SAVE BILLIONS - PAS 91

And, according to the government, PAS 91, a standard prequalification questionnaire for public sector projects, could save the construction industry billions over the next decade. The publicly available specification sets out the nature, content and format of a set of questions relating to the core criteria essential to construction tendering – general supplier information, financial information, business and professional standing and health and safety. It also sets out a standard set of questions for topics of frequent interest to buyers – equal opportunities, environmental management and quality management. The content of the questionnaire will be reviewed after a year. PAS 91 is now available as a free download:

See: http://www.bis.gov.uk/assets/biscore/business-sectors/docs/b/bsi-specification-pas91-construction-procurement.pdf

CHALLENGING A PUBLIC PROCUREMENT AWARD – WHEN DOES THE CLOCK START TICKING?

In issue 60 we reported the court ruling in ***Sita UK Ltd v Greater Manchester Waste Disposal Authority*** that the syndicate challenging the award, by the Greater Manchester Waste Disposal Authority, of the contract for what was said to be the UK's largest PFI waste disposal project, worth £3.8 billion, was too late in bringing proceedings.

The Court of Appeal has now confirmed the original decision and in doing so also had to consider when the three month period for bringing proceedings started to run. This was against the background of the ruling from the Court of Justice of the European Union in ***Uniplex UK Ltd v NHS Business Services Authority*** (C-406/08) [2010] 2CMLR47 that the time limit should run from the date on which the claimant knew, or ought to have known, of the infringement.

So what was the appropriate date of knowledge? The test adopted in the first hearing by Mr Justice Mann for the necessary degree of knowledge was:

".. the standard ought to be a knowledge of the facts which apparently clearly indicate, though they need not absolutely prove, an infringement..."

Two of the Court of Appeal judges adopted this test, with one preferring simply to apply the original Court of Justice formula.

In any event all three judges considered that the proceedings had been brought too late. The syndicate's correspondence established that it knew enough to initiate proceedings more than three months before the time for bringing proceedings expired and that it was making unambiguous assertions to that effect. In addition, contrary to the syndicate's argument, time did not start to run afresh where what is being relied upon to start time running again is a further breach of the same duty, whether it in fact occurred before or after the breaches already known.

See: ***Sita UK Ltd. v Greater Manchester Waste Disposal Authority* [2011] EWCA Civ 156**

Jonathan Olson-Welsh
jolson-welsh@mayerbrown.com

Construction & Engineering Group (UK)

SUPREME COURT GREEN LIGHT FOR LOCAL AUTHORITY MUTUAL INSURANCE ARRANGEMENTS

The 2006 UK public procurement regulations promote the EU principles of fair competition. They seek to prevent the procurement process putting one party at an unfair advantage over others. Public authorities, on the other hand, are free to perform their public duties by using their own administrative, technical and other resources, without being obliged to call on outside entities and without having to go through the procedures prescribed by the regulations. They may also co-operate with other public authorities to ensure that, collectively, they have the necessary resources to perform those duties.

The position becomes more complicated, however, where the authority obtains the services or products it requires from a separate body which, it claims, is so closely connected with it that the authority should still be regarded as obtaining the services or products in-house rather than from an outside body. In this case the regulations do not apply if, and only if, what is intriguingly known as the 'Teckal exemption' applies.

The Teckal exemption started life in a decision of the Court of Justice of the European Union about a corporate entity set up by a consortium of Italian municipalities to provide energy and environmental services to the participating authorities. Teckal, which supplied fuel and serviced heating systems, objected to the decision by one of the municipalities to switch its custom to the consortium entity without complying with the procurement rules. In the hearing of the case, the Court of Justice said that public authority arrangements such as this are exempt from the EU procurement rules:

"...where the local authority exercises over the person concerned a control which is similar to that which it exercises over its own departments and, at the same time, that person carries out the essential part of its activities with the controlling local authority or authorities."

In ***Brent London Borough Council and others v Risk Management Partners Ltd***, the Supreme Court had to decide if the Teckal exemption, and the two tests as to control and function, applied to arrangements for mutual insurance made by a number of local authorities. The arrangements involved the setting up of a company whose business was restricted to the provision of insurance to participating members (i.e. the authorities) or their affiliates and which was funded by participating members and by reinsurance placed in the open market. The majority of the directors were appointed by participating members.

The Supreme Court decided that the Teckal exemption did apply to these arrangements. Collective control of the company was enough to satisfy the first Teckal test as to control, even though it is in the nature of collective control that no single authority could be said to exercise the kind of control which it would have over its own departments.

The second Teckal test, as to function, was designed to ensure that the procurement rules apply unless, in substance, the body concerned only trades with the local authority or authorities (i.e. it is not market-oriented). In ***Brent*** the company only

insured participating members and affiliates (public bodies sponsored by participating members). Since the essential part of the company's activities was with the London boroughs which were participating members, the second Teckal test was satisfied and the arrangements were exempt from the procurement rules.

Which looks like good news for public authorities wanting to set up co-operative arrangements with other authorities to provide necessary services.

Christopher Fellowes
cfellowes@mayerbrown.com

Construction & Engineering Group (UK)

LOOK ON THE BRIGHT SIDE – BUT NOT TOO MUCH?

Optimism is usually a good thing. A glass half full is better than a glass half empty. But sometimes this can cause problems, in particular when forecasting costs and setting budgets, especially when times are hard.

In December last year, budget optimism hit the front pages of The Times, when it focussed on approval of Ministry of Defence budgets for particular projects, only for the budget later to become subject to massive price increases. The Times reported allegations as to a "*conspiracy of optimism*", where, in a reported keenness to get projects approved, those involved were hoping for the best possible outcome when negotiating with industry, rather than accurately forecasting and factoring in appropriate levels of risk. Almost inevitably, unrealistically budgeted contracts ended up costing a lot more once the project was under way.

Optimism in forecasting is not a new concept and has been subject to a number of studies. In 2002 Daniel Kahneman won the Nobel Prize in economics for his theories relating to forecasting. The same year HM Treasury commissioned a report from Mott MacDonald to review large scale public procurement in the UK and the report identified optimism as a source of risk in estimating project costs.

Perhaps the most recent and comprehensive study on the subject is the review undertaken by Professor Flyvbjerg, the BT chair of major project management at Said Business School at the University of Oxford and Professor of Planning at Denmark's Aalborg University. He and his team have researched time and cost overruns around the world on major infrastructure projects that failed to deliver projected results. They asked why this had happened and from the data they collected came up with two main reasons; "*strategic misrepresentation*": an intentional over optimistic estimate on timing, budgets and project benefits for political/economic reasons; and "*optimism bias*": a subconscious predisposition found in most people to judge future events in a more positive light than is warranted by actual experience. The latter sounds not a million miles away from the MOD projects allegations made in The Times.

So can you, and, if so, how do you, deal with optimism bias and strategic misrepresentation? Professor Flyvbjerg's team identified a method of dealing with optimism bias called Reference Class Forecasting. RCF involves predicting a proposed project's performance by looking at the actual performance of a class of similar projects already carried out. These similar projects, according to his team,

are more common than people assume. People often believe their projects are unique, when they are not. Reviewing the average performance of a number of similar projects, they say, can indicate the outcome that might be expected from a proposed similar project. All of which sounds very sensible, so long as you have reliable comparable data for similar projects.

Strategic misrepresentation, on the other hand, is altogether trickier to address, for obvious reasons but, where a misrepresentation induces another party to enter into a contract, there can be legal consequences. ***BSkyb Ltd v HP Enterprise Services UK Ltd*** is an extreme example from 2010; defendants who had won a contract to provide Sky with a new CRM system, so that Sky could provide improved service to its customers at its call centres, had represented to Sky that they had carried out a proper analysis of the time needed to complete the initial delivery and go-live of Sky's call centre. They had also represented that they held (and had reasonable grounds to hold) the opinion that they could and would deliver the project within certain timescales. But the representation was false as there was no "*proper analysis*" nor were there "*reasonable grounds*". It was made dishonestly and was a fraudulent misrepresentation, which entitles a claimant to claim rescission or damages suffered as a result.

Has any one adopted RCF? The HM Treasury Green Book contains some guidance on optimism bias and our very own Department of Transport has taken RCF on board and produced its own Transport Analysis Guidance on the estimation and treatment of scheme costs, which deals, amongst other things, with risk and optimism bias. And for a current example of project planning allowing for optimism bias look no further than the estimate for the proposed Northern Line extension, part of the Vauxhall, Nine Elms, Battersea Development Infrastructure Funding Study.

In these times of austerity, in the hunt for that elusive creature, efficiency savings, will the adoption of RCF (where data permits) by other Government departments, increase in line with the HM Treasury Green Book guidance? Could RCF mean an end to optimistic budgeting, cost overruns and hitting the headlines– or is that being too optimistic?

Wisam Sirhan
WSirhan@mayerbrown.com

Richard Craven
RCraven@mayerbrown.com

Construction & Engineering Group (UK)

PAIN IN SPAIN – FOR THE PROCUREMENT LAWS

Equality, transparency and non-discrimination are fundamental principles of EU procurement. Spanish procurement laws, however, have hit problems with all three. Pablo Silván, a partner in our Alliance firm, Ramón y Cajal Abogados, in Madrid, who specialises in Administrative Law and Regulated Sectors, reports.

Procurement practice prior to 2008

Until Law 30/2007 on Public Sector Contracts came into force in May 2008, Spanish legislation on public procurement (Royal Legislative Decree 2/2000, article 101) stated that once a contract has been awarded the Administration can amend it "*for public interest reasons*" due to "*new requirements*" or "*unforeseen circumstances*".

There is, however, no definition of these "*requirements*" or "*circumstances*" and no limitation on the exercise of this unilateral power (*ius variandi*), other than a requirement to consult the Spanish Council of State or the corresponding regional equivalent if the proposed alteration(s) increase the price by more than 20%. This has given Spanish Public Administrations a wide margin of discretion to amend awarded contracts in order to rectify omissions or defects in the project arrangements or to modify the scope of the works. This flexibility has been even greater when dealing with contracts subject to Spanish private law (i.e. certain agreements awarded by Spanish Public Administrations, as well as contracts awarded by companies in the public sector).

Under the pre 2008 legal regime, over many years, a substantial number of Spanish public works contracts were amended. Contractors asked Public Administrations to amend public works contracts post award, in order to recognise the actual scope of works to be performed (or already performed) and the consequent cost. Public Administrations usually preferred to modify the contracts rather than starting a new tender process, invoking varyingly realistic "*new requirements*" or "*unforeseen circumstances*". Increased prices were usually fixed at less than 20% more than the price of the awarded contract, thus avoiding the Spanish Council of State audit.

In the last few years widespread use of this practice, plus the strong rivalry of Spanish construction companies in the local market, resulted in an increase in bids below the reasonable market price for the provision of works (in some extreme cases more than 40% below the budget forecast at tender stage). This effectively closed the public works market to foreign construction companies, who were not prepared to tender for works below their true cost without any certainty as to the recognition of their real cost.

This approach was particularly criticised by different authorities (not only the European Commission but also the Spanish Council of State) because basic principles of EU Law on public contracts, such as equality and non-discrimination, could have been infringed. The scope of these principles (see article 2 of EC Directive 2004/18/CE requiring equality, non-discrimination and transparency from contracting authorities), as applied to the amendment of contracts, was interpreted by the European Court of Justice in its 29 April 2004 ruling (C-496/99 P, ***Commission v. CAS Succhi di Frutta S.p.a.***).

The Court said (see paras 115 to 125) that all contracting authorities should comply strictly with their own criteria, not only in the tendering procedure itself but also until completion of the relevant contract. Contracting authorities may not alter the general scheme of the invitation to tender by subsequently unilaterally amending an essential condition of the award, in particular if it is a condition which, if included in the notice of invitation to tender, would have given tenderers an opportunity to submit a substantially different tender. Should a contracting authority wish, for particular reasons, to be able to amend conditions of the invitation to tender, after the successful tenderer has been selected, it must provide for that possibility in the notice of invitation to tender and define the framework within which the procedure must be carried out, so that all the undertakings interested in taking part in the procurement procedure are aware of this possibility.

If this possibility is not expressly provided for, the contracting authorities cannot, after the contract has been awarded, derogate from the essential conditions specified. If they could freely amend the invitation to tender conditions, in the absence of express provisions to that effect, this would distort the terms of the original contract award. This practice would also inevitably lead to infringement of the principles of transparency and equal treatment.

The 2007 regime

Until March 2011, Spanish Law 30/2007 on Public Sector Contracts stated in article 202, applicable to administrative contracts, that, once a contract has been executed, the contracting authority, while observing its essential terms and conditions and duly justifying and recording the need to do so, may amend it for reasons of "*public interest*" and to deal with "*unforeseen circumstances*". A new notice of invitation to tender is, however, mandatory whenever the Administration intends to extend the contract to include an item that cannot be integrated into the original scope of the project by correction, or that can "stand alone" and/or to introduce amendments to achieve objectives other than those listed in the tender documents.

In any event, under Law 30/2007, administrative contracts must contain an express provision regulating the amendment of the conditions of the invitation to tender. The Spanish Consultative Board of Administrative Contracts has stated in its report 43/2008 that, if this provision is included, amendment of the contract is possible regardless of the nature or importance of the terms in question. If, however, such a provision is *not* included, amendment will only be possible on justified grounds of public interest which do not affect the contract's essential terms.

Note that private contracts signed by companies belonging to the public sector are not subject to this regime, but are, however, bound by the principles of equality and non-discrimination.

The European Commission has said that the new provisions in Law 30/2007 on administrative contract amendments do not comply with EU law requirements as they still allow a wide margin of discretion to Spanish Public Administrations. It has referred the matter to the European Court of Justice.

Recent amendments of the 2007 regime

Spanish law 2/2011, on Sustainable Development, has modified Law 30/2007, trying to make the public interest requirements compatible with the transparency and non-discrimination principles.

Since 6 March 2011 Law 30/2007:

- permits amendment of administrative contracts, in the event that this possibility has been anticipated in the specification or the invitation to tender, if the conditions, scope and limits of the permissible alterations (including the maximum amendment to the original contract price and the applicable amendment procedure) are clearly specified;
- permits amendment of administrative contracts, even if nothing is said in the specification or the invitation to tender, if at least one of the following criteria is satisfied and justified:

  - the scope of works is inadequate to meet the administrative needs because of mistakes or omissions in the project or technical specification;
  - the project or technical specification is, or are, inadequate because of objective (geological, hydrological, archaeological, environmental or equivalent) reasons arising after the contract has been awarded *and* those reasons are unforeseeable as a matter of good professional practice;
  - the occurrence of force majeure events that prevent the contract from being performed according to its original terms;
  - the advisability of introducing state of the art technical improvements that only become possible after the award of the contract and which could particularly enhance performance of the contract;
  - the need to adapt the contract's provisions to technical, environmental, urban development, security or accessibility requirements introduced after its award.

  Amendments may not alter the essential tender conditions, and are strictly limited to the introduction of whatever is indispensably necessary to satisfy the specific criterion identified. An amendment would therefore be prohibited if, had it been made at tender stage, other undertakings would have tendered or tenderers would have amended their bids.

- states that whenever a Public Administration intends to introduce an amendment other than those specified above, the executed contract must be terminated and a new tender process initiated. Amendments will therefore no longer be possible to add additional items and/or to enlarge the contract´s scope to meet new objectives.

In the light of the European Court of Justice case law, we cannot be sure that even the revised arrangements will fully comply with the EU principles of equality and non-discrimination.

What is clear, however, is that the modified law and the infringement procedure initiated against the Kingdom of Spain will probably result in the end of excessively low bids and discretional use of *ius variandi* by Public Administrations. This may well be at the expense of an increase in the time needed, in future, to procure public

works, because of the greater stringency required in drafting the project's technical and financial specification.

Pablo Silván, Partner
psilvan@ramoncajal.com
Ramón y Cajal Abogados
Madrid.

What's been happening @ Mayer Brown;

ACE GCC CONFERENCE

In October Raid Abu-Manneh was a speaker at the Association for Consultancy and Engineering GCC (Gulf Cooperation Council for the Arab States of the Gulf) conference in Abu Dhabi. The conference addressed the challenges firms face in the region and also focussed on the increasing opportunities available in the GCC countries. Raid was one of the panel providing a legal guide to the GCC.

SCL (GULF) CONFERENCE

Raid was also a speaker at the SCL (Gulf) Conference in Dubai in March. The conference looked at the main issues arising out of typical construction contracts, such as FIDIC 4th edition.

SYMPOSIUM ON INTERNATIONAL ARBITRATION IN GHANA

In November 2010, Kwadwo Sarkodie attended the Symposium on International Arbitration in Accra, Ghana, hosted by the LCIA African Users' Council and the Ghana Arbitration Centre. The organisers had assembled an excellent line-up of speakers from around Africa, and the symposium was attended by arbitrators, judges, lawyers and other professionals from across the continent and beyond.

The event took place at an important time for arbitration and dispute resolution in Ghana, coinciding as it did with the coming into force of the Ghanaian Alternative Dispute Resolution Act 2010*. This piece of legislation provides for the wholesale revision and updating of the law governing arbitration in Ghana, and reflects the Ghanaian government's commitment to promoting the use of arbitration. The new legislation was reviewed and discussed in detail in the course of the symposium, along with a series of other topical issues concerning arbitration, both in Africa and the wider world. These included arbitration agreements, the composition of arbitral tribunals and the management of cultural issues in arbitrations.

Each subject prompted lively comment and debate, with interesting and thought-provoking contributions from the floor following every talk. The symposium proved to be an excellent forum for the sharing of ideas and viewpoints, and the contributions of attendees and speakers from such a variety of legal and cultural backgrounds made for an enlightening examination of arbitration in Africa today.

*Kwadwo has prepared a detailed analysis of the 2010 Ghanaian Alternative Dispute Resolution Act. If you would like a copy, email or call Kwadwo at KSarkodie@mayerbrown.com or on +44 20 3130 3335.

FEBRUARY 2011 – MINING INDABA

In early February Jonathan Hosie attended this year's Mining Indaba in Cape Town, South Africa. Jonathan was representing the Construction & Engineering Group team who are a key component of the Mayer Brown Mining Group.

The conference is Africa's largest and most significant mining event, dedicated to the capitalisation and development of mining interests in Africa.

CONSTRUCTION NEWS: THE REGULATION REPORT 2011

Chris Fellowes (procurement) and Gillian Sproul (competition) were contributors to the Construction News Regulation Report 2011.

WELCOME TO REBECCA DOWNING, RYAN FORDHAM, JAMES MORRIS, DEBBI SIMON AND SAMI ZAMAN

Associates Rebecca, Ryan, James, Debbi and Sami recently joined the London Construction & Engineering Group. We are delighted to welcome them all to the team.

Concurrent delay – Scottish and English courts part company

Time and money delay claims are a traditional battleground of construction disputes. The fighting can also be prolonged and expensive. So the arrival last year, in Scotland, of a case that could have provided the Holy Grail of an answer on the thorny issue of concurrent delay prompted much excitement and set off an avalanche of comment. But did it find the answer?

The fifth Scottish judgment in ***City Inn Ltd v Shepherd Construction Ltd*** appeared just eleven years after practical completion and involved 13 days of hearing and 17 grounds of appeal. So it ought to have been good. Lord Osborne's majority judgment produced five propositions for applying the relevant extension of time machinery in the 1980 JCT standard form. In a nutshell they were:

- for any extension of time claim to succeed, it must be shown that a Relevant Event is a cause of delay and that completion of the works is likely to be, or has been, delayed by that Relevant Event;
- causation is a question of fact to be resolved by applying common sense;
- the decision-maker can decide a causation issue on the basis of any factual evidence acceptable to him. A sound critical path analysis may help but its absence may not be fatal;
- if a dominant cause can be identified as the cause of a delay, immaterial causes of delay can be ignored; success of the time claim then depends on whether the dominant cause is a Relevant Event;
- if there are two causes of delay, a Relevant Event and a contractor default event, and neither is the dominant cause, the claim will not necessarily fail because it will be open to the decision-maker, approaching the issue in a fair and reasonable way, to apportion the delay between the two events.

Lord Osborne also highlighted the importance of identifying what we mean by expressions such as "*concurrent delay*". He thought the "*broad sense*" was the most

likely to be relevant in applying the JCT clause, meaning that both "*concurrent*" events affected some subsequent event, such as the completion of works, even though they did not overlap in time.

The controversial issue was apportionment. Lord Carloway disagreed with Lord Osborne's approach, which he thought was not justified by the contract. The architect's task was "*...first, to determine whether there is likely to be, or was, delay in the Completion Date caused by a Relevant Event and, secondly, to fix such later date as he considers to be "fair and reasonable"*". If a Relevant Event occurs (no matter when), the fact that the works would have been delayed, in any event, because of a contractor default remains irrelevant. The architect must concentrate solely on the effect of the Relevant Event in the absence of any competing default.

Just months later the English courts had something different to say on the issue. In ***De Beers UK Ltd v Atos Origin It Services UK Ltd*** Mr Justice Edwards-Stuart had to consider concurrency in the context of a contract for development of a software system to support diamond supply chain management. He summarised what he considered to be the law in England on concurrency:

"*The general rule in construction and engineering cases is that where there is concurrent delay to completion caused by matters for which both employer and contractor are responsible, the contractor is entitled to an extension of time but he cannot recover in respect of the loss caused by the delay.*"

This view was unaccompanied by any analysis of the contract extension of time machinery or of the previous case law, in particular Lord Osborne's judgment in ***City Inn***, and his view on apportionment. Which means that, for the moment at least, we have different approaches in Scotland and England. So much for the Holy Grail.

Richard Craven
RCraven@mayerbrown.com

Construction & Engineering Group (UK)

If your US client or customer goes bust – don't make it worse

Insolvency of your client or customer is bad news, even if, these days, it comes as no surprise. But if the client or customer is from the US, it could get worse; you could receive a demand from a US bankruptcy trustee. The loss of future income is bad enough, but many companies trading with US companies are receiving demands for repayment of income for work that had been performed, invoiced and banked months before. To avoid the risk of expensive legal proceedings in the US, suppliers often reluctantly pay up, but is there any way of challenging or reducing these demands?

When a company goes bust in the US the bankruptcy trustee has powers to "*look-back*" 90 days from the date of bankruptcy and every payment made by the bankrupt company during that period is potentially recoverable. In the UK, in order to recover equivalent payments, a liquidator or administrator has to establish that there was an "*intention to prefer*" a creditor or that the transaction was at an "*undervalue*" or "*fraudulent*" on other creditors. The US provision on the other hand operates on a "*strict liability*" basis (i.e. there is no need to prove intention to prefer a creditor etc.) and often there is the risk that the bankruptcy trustee may, in their enthusiasm for an expeditious and economical resolution of the bankruptcy, apply a broad-brush approach to recovering payments.

Bankruptcy trustees (or debtors in possession) in the US frequently commence a wave of preference actions days before the statutory deadline (two years after commencement of the bankruptcy). The degree of investigation and analysis of a particular claim may be relatively low; for example, there may be no demand letter before litigation is commenced and the first notice a creditor receives can be a complaint filed in the bankruptcy court. When a complaint is received demanding repayment of an amount that is relatively small compared to the cost of defending a foreign action, the commercial realities will often favour payment.

The US Bankruptcy Code does, however, provide a number of standard defences ("*safe harbors*") to minimise or remove liability. Potentially the most helpful of these for UK businesses would be "*ordinary course of business*" and "*subsequent new value*". So what do they mean?

THE ORDINARY COURSE OF BUSINESS DEFENCE

A debtor who pays a supplier a debt incurred in the ordinary course of business is clearly not seeking to prefer one creditor over another. "*Ordinary*" will be viewed both in relation to the "*ordinary*" course of dealings with that supplier and in relation to prevailing industry standards. For example, if a credit period has been reduced following solvency concerns or if further supply is suddenly made conditional on payment of outstanding amounts then this would be unlikely to qualify as the "*ordinary*" course of business.

Subsequent new value

A creditor is entitled to deduct any new value provided (in goods and services) from any alleged preferential payment received. This is not, however, straightforward as only the unpaid element of the "*new value*" may be credited against the alleged preferential payment.

CONCLUSION – ACT QUICKLY!

So if an apparently genuine demand for repayment arrives on your doorstep from a US bankruptcy trustee don't just reach for your cheque book. Expensive litigation is not an inevitability. A review of your business relationship, followed by a prompt response and negotiation with the bankruptcy trustee can reduce, or even remove, any liability without you ever having to appear in a US Court. See if you can make sure the bucks stop with you.

Andrew Shaffer
ashaffer@mayerbrown.com
Restructuring, Bankruptcy
and Insolvency Group (New York)

Jeremy Snead
JSnead@mayerbrown.com
Restructuring, Bankruptcy
and Insolvency Group (UK)

RIBA 2010 Appointments – the changes in a nutshell

The RIBA forms of appointment have not been without their critics. In 2005, in ***Munkenbeck & Marshall v Harold***, a court went so far as to describe two of the clauses in SFA/99 as "*unfair and onerous*". In 2007, RIBA published a new set of appointments which were still met with criticism and now the 2010 forms of appointment have attempted to address concerns expressed about the 2007 edition. So what are the main changes in the 2010 forms and have they succeeded in meeting the criticism?

- **Limited right to withhold payment**

  As with the 2007 appointment, the 2010 edition excludes the client's common law or equitable rights of set-off but then goes further and expressly limits the client's right to withhold payment "*unless the amount has been agreed with the Consultant or decided by any tribunal*". This looks likely to be the most controversial development in the new form; it may even prevent the client withholding payment in respect of negligently performed services.

- **Standard of care**

  The benchmark for the consultant is still reasonable skill and care but some 2007 obligations have been removed, such as performing the services in accordance with the client's brief and in accordance with project procedures.

- **Termination**

  The provisions for termination have been revised to give the consultant "*equal rights*" to those offered to the client. In practice, this gives the consultant the right to terminate at will by giving "*reasonable notice*", wider than the 2007 edition which limited the right of termination to specific situations, such as a prolonged period of suspension. Termination does not affect the client's copyright licence, presumably allowing a replacement consultant to pick up the design where the outgoing consultant left off.

  Do not be surprised, however, if clients remove the consultant's termination at will option or amend the terms of the appointment so as to pass responsibility to the consultant for any additional costs and delays arising from an at will termination.

- **Cap on liability and net contribution**

  The consultant's liability is limited to the PI cover amount agreed in the appointment (provided it has notified its insurer of the relevant claim as required by the policy). In contrast, the 2007 edition simply allowed the parties to agree a cap on liability.

  The 2010 edition retains a net contribution clause in the body of the appointment.

- **Interest for late payment**

  The 2010 edition sets a higher rate of interest for late payment, 8% above the Bank of England's base rate (in contrast to 5% under the 2007 edition and, interestingly, 8% under SFA/99). In addition, the consultant is entitled to claim its reasonable costs of obtaining any late payment.

- **Language**

  Happily for many commentators, the 2010 form has abandoned the NEC style language.

- **Legislative updates**

  The 2010 edition also includes changes reflecting recent legislative developments.

Most of these changes may not silence the critics who say that the balance of risk under the RIBA form of appointment favours consultants over clients, at least when compared with other forms of appointment, such as the NEC3 Professional Services Contract. As we have seen before, lawyers acting for clients can be expected to amend the terms of the appointment to change the balance of risk.

Chris Wright
Chris.Wright@mayerbrown.com

Construction & Engineering Group (UK)

Case notes

SUBCONTRACTOR CLAIM FAILS FOR LACK OF WRITING

When the new Construction Act comes into force, the adjudication and payment provisions of the amended original Construction Act will apply to oral contracts. Until then, as ***Rok Building Ltd v Bestwood Carpentry Ltd*** has just reminded us, *all* the terms of a construction contract must be in (or evidenced in) writing for the original Act to apply.

A subcontract dispute over the contractual arrangements for joinery and carpentry work involved an excursion to the court, after an adjudication had been started, to find out whether the parties had entered into a construction contract which was all in writing, so that the original Construction Act applied. No, said the judge, they had not and the adjudicator therefore had no jurisdiction. There can be a construction contract in writing even if the actual price is not in writing, for example where a formula for determining the price has been agreed, but if the price is *agreed* orally but not evidenced in writing, then an agreed term is not in writing and the contract is

not a construction contract in writing. The judge also indicated that the existence of *implied* terms, for instance as to reasonable rates or prices, did not prevent a contract being a construction contract in writing.

Rok Building Ltd v Bestwood Carpentry Ltd [2010] EWHC 1409

NOTICE OF DISSATISFACTION – MAKE SURE YOU SEND IT TO THE RIGHT ADDRESS

NEC2 Core Clause 93.1 says that a party dissatisfied with an adjudication decision who wants to refer the dispute to arbitration, must serve notice of intention to refer the dispute to arbitration within four weeks of notification of the adjudicator's decision (or of the time when it should have been notified, if no decision is given in time). Core Clause 13.2 says that a communication has effect when received at the last address notified by the recipient for receiving communications (or that in the Contract Data). In ***Anglian Water Services Ltd v Laing O'Rourke Utilities Ltd*** AWS's solicitors sent notice of intention to refer and notice of arbitration to LOR's solicitors, who then passed the notices to their clients within the time limit. LOR subsequently claimed that the notice of intention to refer had been sent to the wrong address and, therefore, not in accordance with the notice Core Clause. But, even if they were right, did that matter, as LOR had actually received the notice in time?

Yes it did, said the judge. Compliance with the delivery mode specified in clause 13.2 was the only way to achieve effective delivery because the communication only took effect when received at the prescribed address. The probable commercial purpose of the clause was to enable each party to work on the basis that all contract communications would be channelled through one office, to enable every incoming document to be properly filed and its arrival recorded. As it turned out, the Clause 93.1 notice had been effectively served because the judge found that LOR's solicitors had notified their address as the Clause 13.2 address.

Anglian Water Services Ltd v Laing O'Rourke Utilities Ltd [2010] EWHC 1529

HOW MUCH DOES IT COST TO STOP A TRAIN?

Recovery of economic loss caused by negligence is a sensitive legal issue, but what if the economic loss is consequent upon physical damage? The defendants to two claims brought by Network Rail had, separately, damaged overhead rail power cables and caused an accident on a railway bridge that caused railway lines to be closed for significant periods. Liability for the remedial works was accepted but could Network Rail also recover the costs it had to pay to the train operating companies under their franchise agreements because of the disruption?

Yes, they could, said the judge. In negligence cases involving physical damage to a claimant's property, loss of use, profit or revenue can be recovered as damages, subject to establishing causation and provided it is demonstrably consequential on, and closely associated with, the physical damage and the remedial work. The fact that the loss of use, profit or revenue arises through a contract between the claimant and a third party does not stop it being recoverable.

Network Rail Infrastructure Ltd v Conarken Group Ltd [2010] EWHC 1852 (TCC)

BATTLE OF THE FORMS ENDS IN GOALLESS DRAW

The classic "Battle of the Forms" is a contest between prospective contracting parties to see whose standard terms should apply and, as Lord Denning said, "..*In some cases the battle is won by the man who fires the last shot*". In ***GHSP Inc v AB Electronic Ltd***, however, the parties discovered there was a third possibility.

As so often, performance of the contract arrangements, the supply of sensors for Ford trucks, was carried out before the contractual position had been resolved. A batch of the sensors was defective and, to determine the position on liability, the parties had to ask the court what terms applied. They had both put forward their own terms in negotiations but whose terms applied? Neither, said the court; the contract had been made on the terms implied by the Sale of Goods Act 1979, which were neither party's choice.

GHSP Inc v AB Electronic Ltd [2010] EWHC 1828

VANDALS MESS UP THE CHAIN OF CAUSATION

Powder fire extinguishers can create a terrible mess; which is what happened when vandals set one off in a church. The defendant who sold the church the extinguisher had not warned of the risk but was found not liable to the church's insurers because the church had not shown that a warning would have stopped it buying the extinguisher. The case also raised (though it did not need to be decided) the thorny issue of third parties' actions breaking (or not) the chain of causation. Did the vandals' actions, seven years after the extinguisher was supplied, break that chain?

The one Court of Appeal judge who went on to review the case law on "*new intervening act*", said that they did. The courts, he said, have to make a "*value judgment*" when dealing with "*remoteness of damage*" or "*causation*" and, if those concepts are means of deciding who is to be responsible for things that have happened, then in all cases, the ultimate question is: what is the extent of the loss for which a defendant ought fairly, or reasonably or justly to be held liable.

Chubb Fire Ltd v The Vicar of Spalding [2010] EWCA Civ 981

REASONABLE ENDEAVOURS – HOW HARD DO YOU HAVE TO TRY?

The case about the proposed redevelopment of Chelsea Barracks put the Prince of Wales's intervention in the headlines but it also raised other legal issues, in particular the recurring and awkward question of the meaning of "*reasonable endeavours*". In relation to the obtaining of planning permission (and other things), the purchaser of the project had an obligation to "...*use all reasonable but commercially prudent endeavours..*" but just how hard did it have to try? Must it subordinate its own commercial interests to obtaining the desired result?

The judge said that a requirement to use "*all reasonable endeavours*" did not always require the party with that obligation to sacrifice its commercial interests. The issue was even clearer in the case because the additional contract wording "...*but commercially prudent..*" made clear that the purchaser did not have to sacrifice its commercial interests. It could consider its own commercial interests, but not, however, its political interests, if they were different from its commercial interests, or to the extent that they required commercially imprudent measures.

CPC Group Ltd v Qatari Diar Real Estate Investment Company [2010] EWHC 1535 (Ch)

THAT WAS NEVER A PENALTY...

The issue of whether a liquidated damages clause is really a penalty and unenforceable is a familiar visitor to the courts. In ***Azimut-Benetti SpA v Healey*** an agreement to buy a €38 million yacht was the setting; a clause said that if the builder lawfully terminated the contract it could keep 20% of the contract price, as compensation for its estimated losses, but must return the balance of sums received and the buyer's uninstalled supplies. Was this a penalty?

No, said Mr Justice Teare. The court has to be careful not to set too stringent a standard and must bear in mind that what the parties have agreed should normally be upheld. At least in connection with commercial contracts, great caution should be exercised before striking down a clause as penal. A particular clause may be commercially justifiable, provided that its dominant purpose is not to deter the other party from breach. The purpose of the clause in question was not deterrent and was commercially justifiable as providing a balance between the parties on lawful termination by the builder.

Azimut-Benetti Spa (Benetti Division) v Healey [2010] EWHC 2234 (Comm)

QUANTITY AND QUALITY SURVEYORS?

Quantity surveyors are concerned with quantity not quality - or are they? In ***Dhamija v Sunningdale Joineries Ltd*** homeowners claimed that quantity surveyors they had appointed for the construction of their house owed them an implied duty "*...to only value work that had been properly executed by the contractor and was not obviously defective*". The quantity surveyors asked the court to strike out this claim; they said they owed no such duty.

Mr. Justice Akenhead referred to the leading case on quantity surveyors' duties, ***Sutcliffe v Chippendale & Edmondson,*** which said that "*...everyone agreed that the quality of the work was always the responsibility of the architect and never that of the quantity surveyor...*" There was no formal written contract in ***Dhamija*** but the judge found an implied obligation on the quantity surveyors to "*..act with the reasonable skill and care of quantity surveyors of ordinary competence and experience when valuing the works properly executed for the purposes of the interim certificates*". He could not, however, see any basis for the positive duty alleged and thought the defective work claim against the quantity surveyors unsustainable. Despite that, he did not strike out the claim but ordered a preliminary issue, to consider the valuation process and how, if at all, it might be in breach of the implied obligation he had identified.

Dhamija v Sunningdale Joineries Ltd [2010] EWHC 2396

ARE WITHOUT PREJUDICE DISCUSSIONS ALWAYS A CLOSED BOOK?

The Supreme Court's judgment in ***Oceanbulk Shipping v TMT*** has provided a helpful analysis of the protection given to without prejudice negotiations. The protection, founded partly in public policy and partly in the agreement of the parties, is now very much wider than it was, historically, but does have a number of exceptions. Lord Clarke dealt with two of ten exceptions, concluding that evidence of what was said or written in without prejudice negotiations should in principle be

admissible, both when the court is considering a rectification claim (based on an alleged common understanding during the negotiations) and also when the court is considering a submission that the factual background relevant to the true construction of a settlement agreement includes evidence of an objective fact communicated in the course of the negotiations.

Oceanbulk Shipping & Trading SA v TMT Asia Ltd [2010] UKSC 44

HOW TO SPOT A REPUDIATION – BUT IT'S NOT EASY.

Claiming that the other contracting party has repudiated the contract, accepting the repudiation and so bringing its further performance to an end, is dangerous. Get it wrong and you may find you have repudiated the contract. But how do you know what is a repudiation? In ***Eminence Property Developments Ltd. v Heaney*** a property seller miscalculated the notice period for a notice to complete and served formal notice of rescission too early. In deciding that the premature rescission notice was not a repudiation, the Court of Appeal said that the legal test for repudiatory conduct is whether, looking at all the circumstances objectively, from the perspective of a reasonable person in the position of the innocent party, the contract breaker has clearly shown an intention to abandon and altogether refuse to perform the contract. All the circumstances, it said, must be taken into account insofar as they bear on an objective assessment of the intention of the contract breaker; motive may be relevant but is not in itself decisive. The issue is highly fact sensitive, comparison with other cases is of limited value and, although the test is simply stated, applying it to the facts of a particular case may not always be easy.

Eminence Property Developments Ltd. v Heaney[2010] EWCA Civ 1168 and Oates & Anor v Hooper [2010] EWCA Civ 1346

SUB-SUB-CONTRACTOR NOT LIABLE IN TORT FOR DAMAGE TO THE "THING"

Insulation work to chilled water pipework was poorly detailed and executed; the vapour barriers failed and the resulting condensation caused extensive corrosion. The tenants of the premises brought proceedings against the main contractor and services subcontractor in contract under warranties they had given, and the subcontractor claimed contribution from the insulation sub-sub-contractor. A key legal issue, at the heart of this contribution claim, on which there is very little direct case law, was whether the sub-sub-contractor owed the tenants any tort duty of care. Does someone who carelessly instals or manufactures a component, causing damage to the thing or installation of which it is merely a component, owe a duty of care in tort to a third party? In this case the answer was no. The insulated chilled water pipework was essentially one "thing" for the purposes of tort. Insulation was a key component of chilled water pipework, but still only a component, and the absence of a tort cause of action for the tenants was not unreasonable. They (or people in their position) could protect themselves, as they had, by obtaining contractual warranties from relevant parties.

Linklaters Business Services v McAlpine Ltd & Ors [2010] EWHC 2931

AFTER THE EXECUTION - WHAT DOES ESCROW MEAN?

Persia Petroleum Services plc, a provider of oil and gas services to the petroleum industry, commissioned a marine oil exploration survey from Silver Queen Maritime Limited. When PPS failed to pay for certain work, Silver Queen withheld data and issued proceedings. The parties negotiated a settlement, PPS executed the settlement deed and its solicitors sent it to Silver Queen's solicitors for execution. PPS then discovered that Silver Queen had told PPS's ultimate client that it would accept less than the sum PPS had agreed to pay and tried to withdraw from the settlement. Was it too late?

Yes, said the court. A signed and sealed deed can be delivered as an escrow, irrevocable but not taking effect unless and until the condition(s) of the escrow are fulfilled. As the only conditions upon which the settlement deed was delivered, that it was to be signed for Silver Queen and sent back to PPS's solicitors, had been met, the deed took effect. And, despite PPS's argument to the contrary, parties negotiating an agreement to settle hostile litigation generally do not owe duties of disclosure to each other.

Silver Queen Maritime Ltd v Persia Petroleum Services Plc [2010] EWHC 2867

THE UNSTOPPABLE ADJUDICATION

An adjudicator's reasons for her decision included a finding that SMM7 did not apply under the relevant subcontract but, in a second adjudication, the respondent claimed that it did and the second adjudicator decided that she was not bound by the first adjudicator's finding. The adjudication claimant applied for judicial review of the second adjudicator's "decision". It claimed that the first adjudicator's decision on SMM7 was temporarily binding on the parties.

Rule 38 of the TeCSA rules that applied says that (except for bad faith on the adjudicator's part) a party cannot make any application to the courts whatsoever in relation to "*the conduct of the adjudication*" or the decision of the adjudicator until the adjudicator has made (or refused to make) their decision and until the party making the application has complied with the decision. The Scottish court said that "*the conduct of the adjudication*" should be given a wide interpretation and that Rule 38 was a contractual bar to the court proceedings. Quite apart from that, the claimant's case was weak. The referral notice defines the issues that the referring party seeks to have determined but neither it, nor the notice of adjudication, identified the applicability of SMM7 as a dispute and the first adjudicator did not decide that issue. Her view of the issue was simply part of the reasoning in reaching her decision as to the sum due.

In the Petition of W.H.Malcolm Ltd at
http://www.scotcourts.gov.uk/opinions/2010CSOH152.html

AND DO ARBITRATORS GO ON FOR EVER?

What if you settle an arbitration, except for costs, which you leave to the arbitrator, but there is then a dispute as to whether defects were excluded from the settlement. Can the arbitrator deal with the new issue or has their power gone – are they "*functus officio*" as the Latin tag goes? In ***Dawes v Treasure***, Mr Justice Akenhead

referred to arbitration law and practice and drew two conclusions:

- since arbitration is usually consensual, it is first necessary to look at the contract appointing the arbitrator to determine what the parties have agreed, expressly or by implication, as to when an arbitrator's jurisdiction becomes exhausted;
- the settlement of a dispute referred to arbitration, before any final award, does not generally, and certainly does not necessarily, end the arbitrator's jurisdiction. Section 51 of the 1996 Arbitration Act suggests a jurisdiction continuing, after settlement (and not expressly limited by statute), to terminate the substantive proceedings and to deal with costs or other matters still in dispute.

The arbitrator in question did retain unqualified jurisdiction, after the settlement agreement, to decide whether it dealt with the defects alleged, and he decided, correctly, that it did.

Dawes v Treasure and Son Ltd [2010] EWHC 3218 (TCC)

DUTIES OF CARE – AGREE ONE, GET ONE FREE?

A contractor or subcontractor may owe its client a duty of care in contract but does it owe a concurrent duty in tort? It can make a difference, which is why Mr Robinson went to the Court of Appeal. His claim in respect of a defect in his gas flues, discovered 12½ years after completion, would fail if the answer was no, because the claim in contract was out of time.

Lord Justice Jackson said that there is a limited duty to take reasonable care to protect the client against personal injury or damage to other property but duties of care in tort, co-extensive with their contractual obligations, do not "*spring up*" between the parties unless there is an assumption of responsibility. In professional appointments there is commonly an assumption of responsibility which generates a duty of care to protect the client against economic loss but in building contracts it is necessary to look at the relationship and dealings between the parties to ascertain whether the contractor or sub-contractor "*assumed responsibility*" to the other party. In this case the court found no as

Robinson v P.E.Jones (Contractors) Ltd [2011] EWCA Civ 9

REMIND ME – WHAT IS "CONSEQUENTIAL LOSS"?

Over the years, disputes about the meaning of consequential loss have been a familiar feature of the court law reports. In ***McCain Foods GB Ltd v Eco-Tec (Europe) Ltd***, the latest addition to the list, equipment for removing hydrogen sulphide from biogas from potato waste, so that a Combined Heat and Power plant could then turn the biogas into electricity, did not work. Eco-Tec accepted liability for the cost of replacement equipment but resisted all McCain's other claims, notably the cost of acquiring electricity which would have been generated by the new system, had it worked, and the loss of revenue from Certificates of Renewable Energy Production that McCain would also have obtained. Eco-Tec said these claims were " *indirect, special, incidental and consequential damages* " for which the contract stated it had no liability.

The judge referred to the Court of Appeal rulings that "*consequential loss*" is confined to loss or damage within the second limb of ***Hadley v Baxendale***, i.e. loss or damage *not* resulting directly and naturally from the breach of contract complained of and which can only be recovered by reason of the defendant's knowledge of the special circumstances surrounding the contract. The electricity costs, the loss of the ROCs and McCain's other claims were all *direct* losses and therefore not caught by the contract exclusion.

McCain Foods Gb Ltd v Eco-Tec (Europe) Ltd [2011] EWHC 66 (TCC)

PROCUREMENT MODEL ANSWERS – FOR WHOSE EYES ONLY?

Confidentiality is starting to become a regular battleground in procurement challenges. In ***Mears v Leeds City Council***, an unsuccessful tenderer for social housing capital improvement and refurbishment works, wanted to see the Council's model answers against which the tenders were to be assessed. The council said they were confidential but the tenderer asked the court to order disclosure.

The judge treated the model answers as confidential but said that did not prevent them from being disclosed. The ultimate test is whether disclosure is necessary for disposing fairly of the proceedings, subject to any special measure to protect confidentiality. Disclosure of the model answers was necessary for disposing fairly of the proceedings and determining whether there were criteria, sub-criteria or weightings in the model answers which were not disclosed to tenderers. To preserve confidentiality, however, disclosure was restricted to named solicitors and counsel for the tenderer and, if they saw grounds for contending the answers should have been disclosed, to a nominated representative of the tenderer with no previous or future involvement in the procurement (to instruct the lawyers), to whom the council had no reasonable objection.

Mears Ltd v Leeds City Council [2011] EWHC 40.

ON-DEMAND BONDS – BE CAREFUL WHAT YOU ASK FOR.

The good, or bad, thing about on-demand bonds, depending on whether you have received or given one, is that obtaining payment does not require proof of liability under the contract that the bond protects. All that is usually required is an appropriately worded demand accompanied by whatever documents the demand specifies. If, however, the formal requirements are not followed, the bond may not respond. In ***AES-3C Maritza East 1 Eood v Crédit Agricole*** a bond required a demand to contain both a statement to the effect that the contractor had failed to comply with its contractual obligations and any notice to, or claim against, the contractor relating to the relevant breach. The demand made was for €93 million but only enclosed notices or claims in a total sum of some €27million. Was it valid?

No, said the court. It did not comply with the bond requirements because it made a claim for which there was no notice to, or claim against, the contractor. In addition, the sums claimed were not due and payable by the contractor for any breach of obligation relied upon in the demand and were therefore not recoverable under the bond. The contractor also alleged fraud, on the basis that the claimant had

demanded a sum it knew was not due, but the evidence did not support an assertion that the claimant did not honestly believe the demand was correctly made. A mistaken belief that the bond covered prospective loss was no basis for any inference as to dishonesty or fraud.

AES-3C Maritza East 1 Eood v Crédit Agricole Corporate and Investment Bank [2011] EWHC 123 (TCC)

MAY I HAVE A CONTRIBUTION, PLEASE ?

A contractor responsible for the design and construction of offshore works for a gas turbine power station engaged subcontractors for the works, which included excavating a trench for the cooling water system, backfilling and protecting the areas round the intake head and outfall with scour protection to prevent erosion. The contractors also engaged design consultants to design the scour protection. Following scouring around the intake heads, remedial backfilling round the intakes and outfall had to be carried out. The contractors sued the designers, who settled the claim and then sought a contribution from the subcontractors.

To recover a contribution, the designers had to show that they would have been liable to the contractor, assuming that the facts alleged in the contractor's claim were correct, and that the subcontractors were liable to the contractor for the same damage. The court found that the relevant damage was scour caused by reduced scour protection caused by the designers' design failure and the subcontractors' workmanship defects. Since both breaches caused the same damage the court was empowered to award the designers a "just and equitable" contribution and as the design failure had the greater degree of fault and contributed to a larger degree to the damage, in terms of inadequate scour protection, the court assessed the subcontractors' contribution at 35%.

Mouchel Ltd. v Van Oord (UK) Ltd. [2011] EWHC 72 (TCC)

WHY SILENCE CAN BE EXPENSIVE

As far as the courts are concerned, it's good to talk - and potentially expensive to keep quiet. ADR, principally conventional negotiation and mediation, is greatly encouraged by the courts and by Lord Justice Jackson in his costs review who said that, if conventional negotiation fails, it is particularly important to pursue mediation in small building disputes. ***Rolf v De Gijerin*** involved a dispute between a builder and homeowner about the construction of a garage and a loft. The parties fell out, the homeowner repudiated the contract and the builder walked off site. In subsequent court proceedings the homeowner, whose claim varied between £44,000 and £92,000, was awarded just £2,500 and the parties ended up in the Court of Appeal arguing about costs. Since the builder had unreasonably rejected round-table discussions and, in the Court's view, negotiation and/or mediation would have had reasonable prospects of success, the Court made no order as to costs, leaving the builder to bear his own costs. Silence, in this case, was not golden.

Rolf v De Gijerin [2011] EWCA Civ 78

About Mayer Brown

Mayer Brown is a leading global law firm with offices in major cities across the Americas, Asia and Europe. Our presence in the world's leading markets enables us to offer clients access to local market knowledge combined with global reach.

We are noted for our commitment to client service and our ability to assist clients with their most complex and demanding legal and business challenges worldwide. We serve many of the world's largest companies, including a significant portion of the Fortune 100, FTSE 100, DAX and Hang Seng Index companies and more than half of the world's largest investment banks. We provide legal services in areas such as Supreme Court and appellate; litigation; corporate and securities; finance; real estate; tax; intellectual property; government and global trade; restructuring, bankruptcy and insolvency; and environmental.

OFFICE LOCATIONS

AMERICAS
- Charlotte
- Chicago
- Houston
- Los Angeles
- New York
- Palo Alto
- São Paulo
- Washington DC

ASIA
- Bangkok
- Beijing
- Guangzhou
- Hanoi
- Ho Chi Minh City
- Hong Kong
- Shanghai

EUROPE
- Berlin
- Brussels
- Cologne
- Frankfurt
- London
- Paris

TAUIL & CHEQUER ADVOGADOS
in association with Mayer Brown LLP
- São Paulo
- Rio de Janeiro

ALLIANCE LAW FIRMS
- Spain, Ramón & Cajal
- Italy and Eastern Europe, Tonucci & Partners

Please visit www.mayerbrown.com for comprehensive contact information for all Mayer Brown offices.

Mayer Brown is a global legal services organisation comprising legal practices that are separate entities (the Mayer Brown Practices). The Mayer Brown Practices are: Mayer Brown LLP, a limited liability partnership established in the United States; Mayer Brown International LLP, a limited liability partnership (regulated by the Solicitors Regulation Authority and registered in England and Wales number OC 303359); Mayer Brown JSM, a Hong Kong partnership, and its associated entities in Asia; and Tauil & Chequer Advogados, a Brazilian law partnership with which Mayer Brown is associated. "Mayer Brown" and the Mayer Brown logo are the trademarks of the individual Mayer Brown Practices in their respective jurisdictions.

This publication provides information and comments on legal issues and developments of interest to our clients and friends. The foregoing is not a comprehensive treatment of the subject matter covered and is not intended to provide legal advice. Readers should seek legal advice before taking any action with respect to the matters discussed herein.

© 2011. The Mayer Brown Practices. All rights reserved.

0200con
March 2011