

DE-RISKING CONSTRUCTION PROJECTS

Liability Discussion Group
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The following powerpoint slides were presented at the Discussion Group on 5 July 2017. The information contained in the slides was current as at the date of presentation, and should not be relied upon after that date. Please seek separate legal or technical advice.

Procuring Successful Construction Projects - Allocation of Risk

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Procuring Successful Construction Projects - Allocation of Risk

Introduction

- Procurement process
- Identifying and allocating risk
- Managing things going wrong
- Dispute resolution
- Conclusion

Procurement process – traditional approach

- CCCS – Designer appointment
- NZS3910:2013 – construction contract
- NZIA SCC – building contract
- FIDIC – rainbow series, Construction (Red Book), Plant and Design Build (Yellow Book), EPC Turnkey (Silver Book), Design-Build-Operate (Gold Book)
- NEC3 – Complete suite of contracts covering all appointments, based on partnering

Pros	Cons
<ul style="list-style-type: none">• Accepted practice	<ul style="list-style-type: none">• Shortage of skilled resources
<ul style="list-style-type: none">• Price and time certainty	<ul style="list-style-type: none">• Inadequate scoping
<ul style="list-style-type: none">• Fair?	<ul style="list-style-type: none">• Inappropriate delivery methods
<ul style="list-style-type: none">• Competitive, giving market pricing	<ul style="list-style-type: none">• Inequitable allocation of risk
	<ul style="list-style-type: none">• Unrealistic time & cost objectives

Procurement Process – cont'd

- Cup won May 1995
- Syndicates to arrive for 2000 defence in August 1997
- Design and construct, with split appointment
 - Enabling legislation
 - Government grant
 - Resource consents
 - Contractor appointment
 - Coastal permit
 - Occupation licences
- Delivered on time and to budget



Identifying and allocating risk

- Undergrounding Hobson Bay sewer
- Earth pressure balance tunnel boring machine
- ITIG Code of Practice for tunneling projects
- Insurance terms
- Geotechnical baseline report
- Unforeseen, not foreseeable based on:
 - Information provided, known or in the public domain
 - Skilled contractor, with experience, expertise and resources
 - Committed to meet its obligations
- Information must have been relied on, and actually cause cost and/or delay



Things going wrong

- Avoidance
- Supply chain management – Chinese steel?
- Scoping
- Delivery methodology
- Risk allocation
- Realistic expectations
- Early identification of potential disputes



Dispute resolution

- Multi-tiered disputes processes?
- Engineer?
- Disputes Boards
- Adjudication – designers?
- Evaluative mediation
- Arbitration

Conclusion

- One size doesn't fit all
- Take time at the start to understand uncertainty and select an appropriate process
- Allocation of risk is only sensible once risk is understood
- Collaborative working relationships, with clear allocation of responsibility
- Effective interim disputes process which parties can have faith in

Emerging Insurance Risks -Defective Building Products

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Emerging Insurance Risks -Defective Building Products

Fire proof cladding

Exterior cladding on high rise buildings:

- **Grenfell Tower, London.** June 2017
- Tragic fire in which 80 people were killed.
- Building was refurbished at a cost of GBP 10m in 2016, including the installation of exterior cladding.
- More than 60 firms were involved in the renovation.
- 24 floors, 127 apartments.
- Similar fires in other cities with modern high rise apartments, including Melbourne and Dubai.
- Cladding may include polyethylene cores or aluminium skins, both of **which can be flammable if specifications are inadequate.**



Source:Wikipediahttps://upload.wikimedia.org/wikipedia/commons/9/9a/Grenfell_Tower_fire_morning.jpg

Emerging Insurance Risks -Defective Building Products

Fire proof cladding

Exterior cladding on high rise buildings:

- **Lacrosse apartments in Melbourne's Docklands** in November 2014
- Devastating blaze but fortunately no deaths.
- Fireproof exterior cladding imported from China did not meet specifications.
- Subsequent audits by Victorian Building Authority (VBA) highlight the huge scale of the problem.
- **Out of 170 new high rise buildings inspected in VIC, 51% failing to meet specification.**



Emerging Insurance Risks -Defective Building Products

Leaky / Mouldy Buildings

Repair bill currently estimated at around \$NZ11bn.

New Zealand:

- Building industry crisis in NZ affecting many buildings built between 1994 and 2004.
- Especially timber framed buildings.
- Especially any buildings with defective exterior cladding systems.

Australia:

In 2014, the Tasmanian government identified their own leaky building syndrome, while Victoria has also established a task force to monitor similar issues.

In the warmer and more humid climates, especially in the Tropics, the constant damp created by humidity creates fertile ground for mould to grow. Many mining communities are struggling with mould infestations.

Australian Building Codes Board has modified the compliance path for weather tightness Performance Requirements, but it remains to be seen how many older buildings will continue to deteriorate and whether the new code is adequately written and enforced.



Emerging Insurance Risks -Defective Building Products

Structural Steel

Steel imported from Asia:

- An increasing amount of steel is being imported from Asia in to Australia.
- Brittle steel could be prone to failure.
- \$450m Huntley bypass – Chinese steel failed tests – NZ 2016.
- Busselton bridges – Vietnamese steel fails tests – WA 2015.
- **What percentage is tested in New Zealand to ensure it meets specification?**



- Kolkata flyover, India, 2016. At least 27 people killed. Primary cause suspected of being failure of bolts, possibly due to brittle steel.

Emerging Insurance Risks -Defective Building Products

Plasterboard

- **Defective Plasterboard imported from China:**
- Low grade fly ash waste used in the plaster composition.
- Multi-billion dollar problem in USA.
- Allegedly Emitting Several Gases:
 - Carbon Disulfide
 - Carbonyl Sulfide
 - Hydrogen Sulfide
- Corrosion of metal
 - Breakdown of electrical equipment
 - Rusting of galvanized nails and truss supports
- Remedy
 - No standard procedure. **Complete re-build of entire interior often required.**
 - Quantities of this plasterboard were imported in to New Zealand.



Emerging Insurance Risks -Defective Building Products

Asbestos

Asbestos in building products imported from China

Some recent examples from Australia:

- Storage tanks at Port Pyrie smelter (The Australian 24 Aug 2016)
- Roof panels at Perth's Children's hospital (ICA 15 July 2016).
- Metal skirting from China at the site of the Queensland Government's Executive Building (ICA 15 July 2016).
- Concrete fibre sheeting used in construction in at least 64 construction sites in Australia (Feb 2016 - Asbestos Safety and Eradication Agency).
- Plasterboard in new buildings in Canberra (Worksafe ACT 2014).



Emerging Insurance Risks -Defective Building Products

Insurance

Classes of insurance affected:

- Construction Insurance (before completion)
 - Property Insurance (after completion)
 - Public Liability (liability of builders and owners)
 - Products Liability (liability of manufacturers, importers, builders)
 - Professional Liability (engineers, project managers, certifiers)
 - Builders Warranty (structural components)
- Rectification of faulty work is usually excluded but fire or collapse would be covered





Managing the Risk in Construction

Construction Professionals

By Kavita Deobhakta, Partner, Morgan Coakle Lawyers

5 July 2017

As always, specific legal advice should be sought. The information in this presentation is provided for general knowledge only.

Main Areas To Cover

- Importance of using standard contracts (IPENZ Short Form/CCCS/NZIA AAS Agreements)
- Client generated contracts – pitfalls:
 - Engagement agreements
 - Third party duty of care agreements



What's the takeaway message?

- Can't de-risk
- Can only 'manage' the risk
- For a professional, best way to manage risk is by clear, written terms of engagement on the accepted documents with no changes or special conditions which conflict with the obligation to exercise reasonable care and skill.

Importance of Using Industry Agreed documents

- Covers main terms needed for engagement but scope must always be considered carefully
- Consultant's obligations specifically worded to be covered by PI insurance
- Includes important liability limitations/exclusions:
 - financial limitation (e.g. SF: \$500K; CCCS: \$2M)
 - consequential loss/loss of profit claims excluded
 - duration of liability limitation (but rider re current CCCS)
 - proportionate liability

Importance of Using IPENZ/NZIA AAS Short Form/CCCS (cont'd)

- Saves time, cost and worry
- Standard consistent use by consultants will assist profession – help keep out overly onerous client generated contracts
- Beware of variations/modifications – can significantly change obligations and create uninsured obligations

Client Generated Engagement Contracts

- Increasing prevalence in last 10 years
- Usually very one-sided, overly onerous, unfair passing of risk to consultant
- Often include variety of performance warranties/guarantees by consultant - but not professional's role
- Big problem/risk – additional obligations not covered by PI insurance which applies to breaches of common law and some statutory obligations

Client Contracts – Common Problems

- Contractual duty of care higher than common law duty
= uninsured liability
- Contractual obligations beyond common law obligations
= uninsured liability
- No or inadequate liability limitations/exclusions
= unwarranted financial exposure

Client Contracts – Common Problems (cont'd)

- Contractual duty of care higher than common law duty:
 - Common Law: skill, care, diligence of a competent consultant exercising reasonable care
 - Contractual examples: “industry best practice”, “expert”, “leading professional”, “world’s best practice”

Client Contracts – Common Problems (cont'd)

- Contractual obligations beyond common law obligations:
 - Performance warranties/guarantees [common trigger words: “warrants”, “covenants”, “guarantees”, “undertakes”, “fit for purpose”]
 - Indemnities = promise to meet client’s full loss due to consultant’s default; often gap between insurance and client’s actual loss/expenses – can be significant [common trigger words: “indemnity”, “indemnify”, “hold harmless”]
 - Extending causation liability – [common trigger words: “liable for loss...in connection with”]

Third Party Duty of Care Contracts

- Create contractual duty of care obligations to non-clients e.g. future owners, tenants, financiers; also to non-client principals or non-client main contractors
- Increasing prevalence in last 5 years
- Various names: Duty of Care Agreement, Collateral Warranty Agreement, Warranty Agreement, Continuity Agreement

Third Party Duty of Care Contracts – Common Problems

- Create duty of care obligation to a party to whom duty is not owed by consultant at common law - so obligation beyond standard PI cover [consultant only clearly owes general common law duty to client, and to future home owner]
- Often include uninsured obligations e.g: higher duty of care standard, performance warranties/guarantees, indemnities, no or inadequate limitations/exclusions
- Can also be “hidden” in Novation Agreements

Third Party Duty of Care Contracts – Minimising Legal Risk/Exposure

- Insurance increasingly available – may need to be a special policy extension and increased premium
- Obligations in third party agreement should be no greater or longer lasting than owed to client under engagement agreement for project
- Consultant's total aggregate liability for project services collectively under engagement agreement and any third party agreements limited as per engagement agreement

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