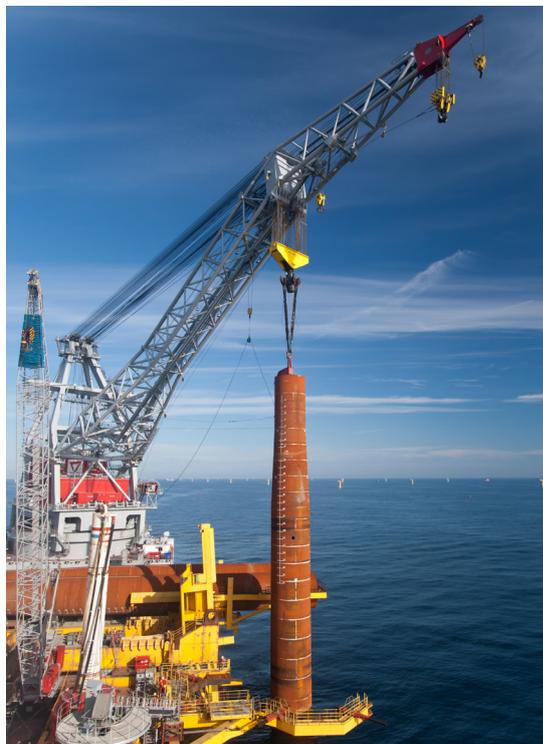


Further information

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Welcome to the June 2014 edition of Quaystone. This month we focus on offshore renewables projects. Increasing activity in the sector over the last few years has meant that disputes have now started to filter through to the courts. We report on some of the most relevant. We also take a look at how to deal with interface risk in package contract procurement - the most common project structure in offshore renewables.

If industry design standards are wrong is the D&B contractor still on the hook?



The recent case of MT Højgaard a/s (“MTH”) and E.ON Climate and Renewables UK Robin Rigg East Limited & Others (“EON”) considered this point. One of our lawyers had the opportunity to sit with the judge throughout the trial and we eagerly awaited the decision.

The judgment has now been published and the simple answer is – as always – it depends on the wording of the contract. The judge decided that MTH was liable to ensure a minimum service life for the works notwithstanding that it had exercised reasonable skill and care when executing the design and had relied on an accepted industry standard that was subsequently found to be defective.

The case related to the design and construction of foundations for sixty wind turbines for the Robin

Rigg offshore wind farm in the Solway Firth. The foundations were formed of a steel monopile and transition piece. The grouted connection between the monopile and transition piece failed causing movement in the structure. The cost of the remedial works was estimated to be around €26.25 million.

The design of the grouted connection was based on an international standard produced by Det Norske Veritas (“DNV”), an independent classification and certification agency. DNV standards are widely accepted by the industry and formed part of EON’s specification for the project. Unfortunately, the standard was wrong. This was only discovered after the project was completed.

The contract required MTH to design and construct the works with the due care and diligence expected of appropriately qualified and experienced designers. In addition, the works were to be designed and constructed in accordance with good industry practice, were required to comply with the specification (including the DNV standard) and to be fit for the purpose set

If the names of the parties in this case sound familiar, that may be because this is not the first time a dispute between them on this project has reached the TCC. In the [June 2013 edition of Quaystone](#) we reported on the judgment on the parties’ case involving the replacement of the vessel used for the foundation installation.

out in the specification. The specification referred to a design life of twenty years and a minimum service life of twenty years.

Who was responsible for the failure? EON argued that MTH had an absolute obligation to ensure a minimum service life of 20 years for the foundations and, in any event, MTH had not used reasonable skill and care

when applying the DNV standard. MTH argued that it was reasonable for it to follow an internationally recognised standard and in doing so had exercised reasonable skill and care.

The two key issues were: (i) was MTH's design obligation limited to complying with the DNV standard or did it assume an absolute obligation to achieve the minimum service life of 20 years; and (ii) could the "absolute" and "reasonable skill and care" obligations exist side by side in the contract? In particular, were the terms concerning "design life" (which required reasonable skill and care) and "service life" (an absolute requirement) compatible?

There is limited case law on the issue but having reviewed largely Canadian authorities the judge found that an absolute warranty can trump a general obligation to comply with the specification. Given the fitness for purpose obligations in the contract, MTH had therefore assumed an absolute obligation to design and construct the works to achieve a minimum service life of twenty years. The grouted connections had plainly failed to achieve such a purpose.

The judge also pointed out that it was not uncommon for construction contracts to contain obligations both to exercise reasonable skill and care (or to do the work in a workmanlike manner) and to achieve a particular result. These were not incompatible. He gave the example of a brick building with a particular design life that was an eyesore because different types of brick had been used in its construction. The bricks may be sufficiently robust individually and collectively to satisfy the design life but the works would fail the workmanship test due to their poor appearance.

The judge added that he could understand why an employer would want a design life (in accordance with the applicable DNV standard) but it was also open for him to stipulate a particular service life. This would usually come at a price as the contractor would have to consider what additional measures he should take to reduce the potential for failure within the service life.

Put simply the judge said that MTH was obliged to (i) exercise reasonable skill and care in preparing the design; (ii) comply with the DNV standard; and (iii) to meet the service life period. MTH complied with the first two obligations but that didn't matter because it failed to comply with the separate, absolute, obligation to meet the service life requirement.

At first the decision may seem unfair on MTH. The failure for which it has been found liable is based in part on its reliance on an international standard which it could not possibly have known was defective when it was undertaking the works. But it is clear from the judgment that the judge simply followed the terms of the contract that MTH had agreed to.

The decision does not establish any new law but does serve as a reminder to contracting parties to exercise care when negotiating and agreeing terms. It confirms that if a contractor accepts separate design obligations to exercise skill and care and to achieve a specific performance standard, compliance with the obligation to exercise reasonable skill and care will not be a defence to a claim arising from a failure to meet the specified performance standard, even if the cause is a defect in an industry recognised design detail.

Multi package contracting: How to deal with interface issues

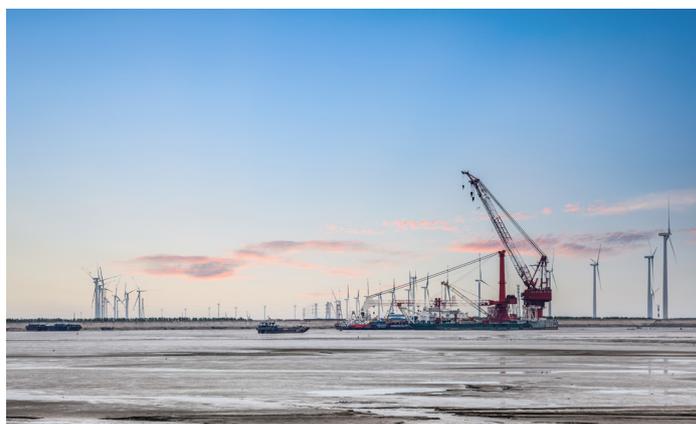
Most offshore renewable energy projects are procured on a multi-contract rather than a single EPC (turnkey) basis. This is generally found by developers to be the most commercially viable procurement solution because it:

- (i) reduces the risk premiums that contractors add to their price as they better understand the delivery risks involved;
- (ii) ensures that each package is delivered by a contractor confident and experienced in delivering works of that nature; and
- (iii) provides a more attractive opportunity to the supply chain thereby encouraging a competitive tender process.

However, this approach does lead to developers (and funders) retaining potentially significant levels of interface risk. Understanding and managing that risk is crucial to the successful outcome of the project (and to the likelihood of it securing funding).

The interface issues that need to be dealt with include:

- Design: the various packages must not only fit together but work together. The interfaces between them must therefore be designed collaboratively by all relevant contractors.
- Programme: both the design and delivery phases need to be coordinated. There must be timely exchange of information to allow the interfaces to be correctly designed and, once on site, the contractors' activities need to be coordinated so that they don't hinder each other.



- Testing: from a developer's perspective it is not only important that the various packages do what they are supposed to individually but that they all work together to meet the project output requirements.
- Disputes: any major disputes that do arise are likely to concern more than one package so common dispute resolution procedures, including joinder provisions (so related disputes with different contractors may be decided together), are essential.

There are, principally, two contractual ways of dealing with these interface issues:

1. an interface agreement between the developer, all package contractors and possibly the employer's engineer; or
2. common interface provisions in all package contracts.

The developer's aim in adopting either of these approaches is to establish contractual mechanisms which allow the interfaces to be managed effectively and robust terms to ensure that contractors comply with them.

Often the developer's (and funders') preferred solution is an interface agreement which requires contractors to sort out between themselves the effects of delay or disruption they have caused rather than channelling claims through the developer. This reduces the developer's administrative burden and insolvency risk. However, it is very hard to negotiate in practice as it leaves each contractor to rely on the ability and willingness of the other contractors to meet any liabilities they may incur under the terms of the interface agreement. This is likely to be less attractive than simply bringing a claim against the developer and leaving the developer to pursue any reciprocal claim against the responsible contractor.

A common compromise is to use a carrot and stick approach in the common interface provisions. A

combination of robust terms providing clear and binding obligations to cooperate and swap information and financial incentives that contractors can only claim if the project as a whole is completed on time and to spec often works well.

Either way, much can be done at the planning stage to minimise risks and then mitigate the risks that remain. Simple steps include keeping the number of packages to a minimum (thereby minimising the number of interfaces), appointing an experienced project manager to manage the interfaces and holding multiple pre-contract meetings between the PM and contractors to develop the design to a high level of detail and familiarise all parties with the operation of the interface provisions.

We have been involved in a number of renewables projects, both onshore and offshore, that have successfully adopted this approach.

Onshore lessons for offshore work

The FIDIC forms of contract, the Yellow Book in particular, are commonly used in the UK for the procurement of offshore construction works. Despite their widespread use, surprisingly few disputes involving FIDIC contracts have reached the English courts. A TCC case published in April 2014 is an exception. Although it concerns onshore works it has implications for any offshore project using FIDIC contracts.

Spanish contractor Obrascon Huarte Lain SA ("**Obrascon**") entered into a contract based on the FIDIC Yellow Book with the Gibraltar government ("**Gibraltar**") for the design and construction of a tunnel under the runway at Gibraltar airport. It did not go well. Two and a half years into the two year contract, with only 25% of the work completed, Gibraltar terminated the contract. Obrascon claimed the termination was unlawful and that it was entitled to an extension of time due to the quantity of contaminated ground found on the site.

The contract provided that Obrascon could claim an extension of time if the ground conditions encountered could not reasonably have been foreseen by an experienced contractor at the tender date. Obrascon relied heavily on reports that Gibraltar provided during the tender process to claim that the extensive contamination (by lead and hydrocarbons) actually encountered was not reasonably foreseeable. The court rejected these arguments. The court found that it was obvious from records that the site for the tunnel had previously been used as a rifle range and then a fuel store. Therefore the type of contamination encountered was entirely foreseeable. The court noted that, "*what was needed and could have been expected from experienced contractors was some intelligent assessment and analysis*".



The court also considered what level of failure on the part of Obrascon would be required to entitle Gibraltar to terminate. It concluded that "*termination must relate to significant and more than minor defaults*". What is significant and what is minor will depend on the particular facts of each case. However, in deciding where the balance should lie, "*a commercially sensible construction [of the contract's terms] is required*". On the facts, Gibraltar was entitled to terminate both because of Obrascon's failure to proceed with the works with due expedition and without delay and because Obrascon had plainly demonstrated its intention not to continue with the performance of its obligations.

Finally, the court found that Obrascon was time barred from making certain of its claims for extensions of time because it had failed to comply with the time period specified in the contract.

This case decided no new law. However, it is useful guidance on how the courts are likely to interpret FIDIC contracts.

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