Key project and procurement concepts

05 Loss and liability

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1
Recovery of loss

1.1 Introduction

Contractors limit their liability to the Principal under or in connection with an infrastructure contract by:

- excluding 'consequential' or 'indirect' losses and/or specific heads of loss
- including liability caps and/or an aggregate liability cap that restricts their overall liability in connection with the project.

The construction, definitions and carve outs associated with these types of clauses are commonly negotiated together and in conjunction with insurance arrangements as the parties seek to reach a compromise between the scope and risk of each party's liability to the other and the application and value of any liability cap.

Each of these concepts are discussed in turn.

1.2 Excluding liability for indirect or consequential loss

It is usual for Principals and financiers to accept drafting that limits the Contractor's liability for 'consequential' or 'indirect' losses under or in connection with an infrastructure contract.

However, this requires careful consideration of the context, construction and wording of a contract to ensure the Principal does not overly or inadvertently restrict its rights to recover various types of loss from a Contractor.

In particular, Principals should be cognisant of the different positions under English and Australian law, as well as between different jurisdictions within Australia, in relation to how courts will interpret the words 'indirect' or 'consequential' loss.

The classification of a particular loss as indirect or consequential at law is difficult to draft in a manner that gives certainty. If there is a particular loss that the Principal wants to be able to recover it should be expressly stipulated.

Position under English law

Under English law, the two limbed principle governing the remoteness of damage for breach of contract was stated by Alderson J in *Hadley v Baxendale* (1854) 9 Ex 341 (**Hadley v Baxendale**). It provides that where a party breaches a contract, the damages to which the other party is entitled are those which may be fairly and reasonably considered:

- to arise naturally, that is, according to the usual course of things, from the breach of contract itself (often referred to as direct loss or damage) (**first limb**), or
- to be in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of contract (often referred to as indirect loss or damage) (**second limb**).[1]

The terms 'indirect' and 'consequential' loss are often used interchangeably in the context of the second limb of this principle, and if they fall within the second limb, then they will be recoverable under the rule in Hadley v Baxendale.

Case law relating to the second limb

It is worth noting that the court took a more expansive interpretation of the meaning of 'indirect and consequential' loss in the case of *2 Entertain Video Ltd & Ors v Sony DADC Europe Ltd*.[2] The court considered whether the plaintiff's claim for loss of profit was precluded by an exclusion in the following terms:

> *Neither party shall be liable under this Agreement in connection with the supply of or failure to supply the Logistics Services for any indirect or consequential loss or damage including (to the extent only that such are indirect or consequential loss or damage only) but not limited to loss of profits, loss of sales, loss of revenue, damage to reputation, loss or waste of management or staff time or interruption of business.*

After the considering the recent judicial criticism of the traditional approach the Court accepted the submission:

> *[…] that any general understanding of the meaning of 'indirect or consequential loss' must not override the true construction of that clause when read in context against the other provisions in the Logistics Contract and the factual matrix.*

However, in evaluating the natural and ordinary meaning of the clause, the judge reached the same conclusion as the traditional approach whereby the lost profits were nevertheless caused as a direct and natural result of the fire at the respondent's warehouse. Nonetheless, this case marks the first attempt in articulating a gradual shift in the judicial opinion towards broadening of the traditional approach to the second limb of Hadley v Baxendale.

1 *Hadley v Baxendale* (1854) 9 Ex 341, 354 (Alderson J).

2 [2020] EWHC 972.

Case law relating to the first limb

The case of *Transfield Shipping v Mercator Shipping Inc*[3] (**The Achilleas**) also introduced the test of assumption of responsibility to the assessment of damages for breach of contract. In this case, a time-chartered vessel (The Achilleas) was delayed and, in breach of contract, was redelivered to the Principal late. The Principal had already agreed a follow-on charter with a third party and, because of the late delivery, they were forced to renegotiate the rate of hire to a substantially reduced rate. The Principal sued for breach of contract claiming damages for the difference between the original and renegotiated hire rates for the entire duration of the follow-on charter.

The majority in the House of Lords took a new approach to remoteness of damages, by introducing an 'assumption of responsibility for the loss' element to the Hadley v Baxendale test. The remoteness test applied was whether the parties had the type of loss within their contemplation when the contract was made and also whether they had liability for this type of loss within their contemplation then. In other words, was the charterer to be taken to have undertaken legal responsibility for this type of loss?

Lord Hoffman said that the 'standard' Hadley v Baxendale test would be applicable in the 'great majority of cases' but that it would not be sufficient in cases 'in which the context, surrounding circumstances or general understanding in the relevant market shows that a party would not reasonably have been regarded as assuming responsibility for such losses'.

Applying the new test in this case, the House of Lords held that although the loss of profits on the charter were foreseeable, the general understanding in the shipping market was that liability was restricted to the difference between the market rate and the charter rate for the overrun period. The charterer had, therefore, only assumed liability for these losses and the House of Lords awarded damages accordingly.

Since this case there has been some uncertainty as to whether the correct remoteness test is the 'orthodox' test in Hadley v Baxendale or the 'assumption of responsibility' test. However, the *High Court in Sylvia Shipping Co Limited v Progress Bulk Carriers Limited* confirmed that Hadley v Baxendale test remains the standard rule of remoteness and it is only in relatively unusual cases such as The Achilleas where a consideration of assumption of responsibility may be required.

Position under Australian law – Peerless approach

Courts in Australia have previously supported the English law position discussed above — that is, that recoverable indirect or consequential loss is loss that was in the contemplation of both parties, at the time the contract was made, as the probable result of the relevant breach of contract.

However, in the case of *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* [2008] VSCA 26 (**Peerless**), the Victorian Court of Appeal moved away from second limb of the principle in Hadley v Baxendale and decided that the term 'consequential loss' should be given its ordinary and natural meaning as would be conceived by ordinary reasonable business persons.[4] In applying this approach, the court drew a distinction between:

- loss that every plaintiff in a like situation will suffer (**normal loss**)
- anything beyond the normal measure of damages, such as profits lost or expenses incurred through breach (**consequential loss**).[5]

Accordingly, the approach in Peerless highlights that indirect or consequential loss, given its ordinary meaning, is no longer consigned to the second limb of Hadley v Baxendale. Rather, indirect or consequential loss may include a range of losses that have historically fallen under the first limb of Hadley v Baxendale. As such, it is increasingly important for a Principal to consider carve outs to any exclusion of liability for indirect or consequential loss to ensure it does not inadvertently preclude the recovery of certain losses.

The approach in Peerless has been considered by a number of lower courts in Australia, but not determinatively by the High Court of Australia.

For instance, in *Alstom Ltd v Yokogawa Australia Pty Ltd (No 7)* [2012] SASC 49 (**Alstom**), the Supreme Court of South Australia considered a clause in a contract which excluded a party's liability as subcontractor to Alstom (the head Contractor) for 'any indirect, economic or consequential loss whatsoever'. In relation to the interpretation of such clauses, consistently with Peerless, Belby J at 281 stated:

> *To limit the meaning of indirect or consequential losses and like expressions, in whatever context they may appear, to losses arising only under the second limb of Hadley v Baxendale is, in my view, unduly restrictive and fails to do justice to the language used. The word 'consequential', according to the Shorter Oxford English Dictionary means 'following, especially as an effect, immediate or eventual or as a logical inference'. That means that, unless qualified by its context, it would normally extend, subject to rules relating to remoteness, to all damages suffered as a consequence of a breach of contract. That is not necessarily the same as loss or damage consequential upon a defect in material where other remedies are also provided.*

In Alstom, the terms of the contract in question required the subcontractor to pay damages if it did not complete the works on time and/or if the works did not meet the performance tests. Alstom made claims against the subcontractor and sought compensation in relation to breaches of these obligations, asserting that the breaches had resulted in losses that flowed naturally from each breach, and therefore were within the first limb of Hadley v Baxendale. The subcontractor disagreed and instead relied upon the exclusion clause, arguing that the clause should be read to include losses that occurred as a consequence of the breach of contract.

3 [2008] UKHL 48.

4 *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd* [2008] VSCA 26, [93] (Nettle JA, Ashley JA and Dodds-Streeton JA agreeing).

5 Ibid, [87] (Nettle JA, Ashley JA and Dodds-Streeton JA agreeing).

Importantly, the contract did not carve out the recovery of liquidated damages and performance guarantee payments from the exclusion of indirect or consequential loss.

The Supreme Court of South Australia considered these arguments, and held that although the losses claimed by Alstom fell within the first limb of Hadley v Baxendale, the breadth of the exclusion clause meant that the subcontractor was not liable for damages occurring as a consequence of any breaches of contract. The court stated at 290:

> *The expression 'indirect … or consequential loss' appears, in this case, as part of a freestanding and powerfully expressed exclusion clause. It is not affected by the immediate presence of any concession as to liability which it might qualify, although it must be read against the background of the qualified exposure of [the subcontractor] to the exclusive remedies of Liquidated Damages and reimbursement of Performance Guarantee Payments. The Article in question was intended to operate in respect of potential liability for loss incurred by Alstom, which was caused by a breach of contract by [the subcontractor] in circumstances other than those giving rise to the payment of Liquidated Damages and reimbursement of Performance Guarantee Payments. The words must be given their ordinary and natural meaning. In those circumstances any loss consequential or following, immediate or eventual, flowing from a breach of contract by [the subcontractor] is excluded from recovery by Alstom.*

The Peerless approach has also been considered or applied in more recent decisions of the Supreme Court of NSW and the Federal Court of Australia.[6]

Position under Australian law – Regional Power approach

On the other hand, in *Regional Power Corporation v Pacific Hydro Group Two Pty Ltd (No 2)* [2013] WASC 356 (**Regional Power**), the Supreme Court of Western Australia opted against both the English law position and the Peerless approach because of their rigid adherence to classification. Instead, the court held that clauses excluding consequential loss should be construed in accordance with the circumstances of the case and the natural and ordinary meaning of the contract:

> *To reject the rigid construction approach towards the term 'consequential loss' predicated upon a conceptual inappropriateness of invoking the Hadley v Baxendale dichotomy as to remoteness of loss, only then to replace that approach by a rigid touchstone of the 'normal measure of damages' and which always automatically eliminates profits lost and expenses incurred, would pose equivalent conceptual difficulties. Accordingly, I doubt whether the [93] observations in [Peerless] were intended to carry any general applicability towards establishing a rigid new construction principle for limitation clauses going much beyond the presenting circumstances of that case.*[7]

This case concerned a power purchase agreement between Regional Power (as offtaker) and Pacific Hydro (the asset owner) for the supply of electricity from the Ord Hydro Power Station. The power station suffered an outage which resulted in flooding and led to the power station being inoperative for two months. As a result, Regional Power claimed damages for breach of the agreement consisting of costs relating to the hiring of replacement diesel generators, cranes and fuel required to run the extra generators, as well as wages, travel, accommodation and meal expenses of the additional operators required during that period.

Pacific Hydro argued that the damages claimed by Regional Power were indirect or consequential losses and therefore excluded from recovery by the following exclusion clause:

> *Neither [party] shall be liable to the other party in contract, tort, warranty, strict liability, or any other legal theory for any indirect, consequential, incidental, punitive or exemplary damages or loss of profits.*

The Supreme Court of Western Australia held that costs incurred by Regional Power in relation to the replacement power generation and associated outlays constituted a direct economic loss and therefore were not excluded from recovery by the exclusion clause.[8]

In reaching this position, the Supreme Court of Western Australia emphasised the earlier High Court of Australia authority of *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500 which provides that an exclusion clause must be given its natural and ordinary meaning within the context of the contract as a whole.[9] In this respect, the court stated:

> *Construing [the exclusion clause] within the [agreement] as a whole, the court should not be artificially fettered towards assessing the character of an economic loss by rather vague criteria of whether or not the loss arose 'in the ordinary course of things'. Nor should the court be oriented from the start towards trying to determine if a claimed loss falls under the equally porous concept of a 'normal measure of damage'.*[10]

Implications for infrastructure contracts

In summary, there are now three different approaches used to determine the meaning of the words 'indirect' or 'consequential' when used in an exclusion or limitation of liability clause:

- the **English approach**, where 'indirect' or 'consequential' loss are construed as a reference to the second limb of Hadley v Baxendale resulting from the special circumstances under which the contract was made and communicated by one party to the other

6 See for example, *Macmahon Mining Services v Cobar Management* [2014] NSWSC 731, [14]; *Sherrin Hire Pty Ltd v Tidd Ross Todd Ltd (No 2)* [2016] FCA 891, [19]-[20].

7 *Regional Power Corporation v Pacific Hydro Group Two Pty Ltd (No 2)* [2013] WASC 356, [96].

8 *Regional Power Corporation v Pacific Hydro Group Two Pty Ltd (No 2)* [2013] WASC 356, [117]-[118].

9 *Darlington Futures Ltd v Delco Australia Pty Ltd* (1986) 161 CLR 500, 510.

10 *Regional Power Corporation v Pacific Hydro Group Two Pty Ltd (No 2)* [2013] WASC 356, [116].

- the **Peerless approach (Victoria, New South Wales and South Australia),** where 'indirect' or 'consequential' loss can be recovered under the first limb of Hadley v Baxendale if they are a consequence of the breach, and, for example, may include loss of profits
- the **Regional Power approach (Western Australia),** where 'indirect' or 'consequential' loss and damage are said to refer to losses that are in some ways less direct and more removed when considered in the context of the transaction at hand.

Each of these approaches can create uncertainty for a Principal looking to recover a range of damages from a Contractor following a breach of contract.

1.3 Suggested sample drafting

In Australia, with the Peerless approach creating scope for recovery of losses historically classified as indirect losses to be considered as direct losses, the response by Principals and Contractors alike has been to tighten the drafting of exclusion clauses — instead of simply excluding the broad category of indirect and consequential loss, clauses now commonly specify in detail those losses which are to be specifically excluded.

The advantage of this drafting approach is that it forces the parties to address, prior to entering into the contract, those consequential or indirect losses it wishes to be able to recover, and those which it might be prepared to negotiate as excluded losses. This drafting can also be adopted in those jurisdictions which follow the English approach as a way to add further legal and commercial certainty.

Drafting example: Exclusion of liability for Consequential Loss

1. *'Neither party will be liable to the other party in any circumstances for any Consequential Loss.*
2. *For the purpose of clause 1, "Consequential Loss" means:*
    a. *any Loss that does not flow directly and naturally from the relevant breach of this Agreement or a duty of care*
    b. *any loss of financial opportunity, profit, anticipated profit, business, business opportunities, revenue, reputation, income, funding or goodwill, in each case, irrespective of whether direct, indirect or consequential.'*

1.4 Carve outs to the exclusion of consequential loss

For a Principal agreeing to exclude consequential loss under an infrastructure contract, it is important to consider whether there should be any carve-outs to this exclusion, such that certain types of consequential or indirect loss are still recoverable.

The carve outs are often the same as or similar to the carve outs to the liability cap (discussed in section 1.5) as they are consistent with the risks which the Contractor has agreed to bear more broadly under the contract without limitation. Addressing appropriate carve outs is also important to ensure that losses intended to be recoverable that would otherwise be considered indirect or consequential (such as those covered by delay liquidated damages or performance liquidated damage) are not inadvertently excluded from the Contractor's liability to the Principal.

Drafting example: Carve outs to Consequential Loss exclusion

'Consequential Loss does not include the following (which are Direct Loss):

a. *Loss that the Principal is entitled to recover pursuant to an express term of this Contract*
b. *Performance Liquidated Damages*
c. *Delay Liquidated Damages*
d. *damages at law under clause [insert reference to the clause which entitles the Principal to damages at law for delay and breach of performance guarantees if the relevant liquidated damages regimes are held to be void or unenforceable]*
e. *costs incurred by the Principal under clause [insert reference to the clause which requires the Contractor to pay the Principal's costs of completing the works if the performance guarantees have not been met by the time the delay liquidated damages cap has been exhausted]*
f. *Loss that would have been covered by insurance held by either the Contractor or the Principal under clause [insert reference to the clause which sets out the requirements for insurance] but for a breach of that clause or the terms of those insurance policies by the Contractor*
g. *Loss arising from fines or penalties levied by any government authority for breach of any law by the Contractor*
h. *Loss arising from the Contractor's fraud, wilful misconduct, corrupt acts or omissions or unlawful acts*
i. *Loss arising where the Contractor abandons the works or repudiates this Contract*
j. *Loss to the Principal covered by clause [insert reference to the clause which requires the Contractor to take care, custody and control of the Works and the Facility until the Date of Commercial Operations]*
k. *Loss incurred by, or claims brought against, the Principal under any Project Approval as a direct result of a breach by the Contractor of its obligations under this Contract*
l. *Loss arising from any breach by the Contractor under clauses [insert reference to the clauses which deal with confidential information and intellectual property]*
m. *Loss arising from the Contractor's liability under clauses [insert reference to the clause which requires the Contractor to pay the Principal's costs of repairing the Facility where the Contractor has failed to do so or to make the Facility meet the performance guarantees]*
n. *Loss incurred by the Principal following termination of this Contract under clauses [insert reference to the clauses which entitle the Principal to terminate the Contract if either of the sub-caps for Delay Liquidated Damages or Performance Liquidated Damages is met].'*

As discussed in relation to carve-outs to liability caps, it is also common for Principals to carve out from the exclusion of consequential loss any payments recovered or recoverable under insurances taken out in accordance with the contract. This is discussed further in section 1.5 and a similar analysis applies here.

1.5 Liability caps

Drafting issues

The following matters must be considered:

- Is it a cap on all liabilities or just some?
- Is it an aggregate/overall cap or are there sub-caps which apply to specific liabilities. For example, a cap on the liability for liquidated damages?
- Is it a cap on the liabilities under the contract only or at law as well (for example, tort)?
- What is the size of the cap? Is it a lump sum figure or is it expressed as a percentage or multiple of the contract price?
- Are there any 'carve-outs' or exceptions to the liability cap (for example, liabilities that are not covered by the cap)?

Quantum

Despite the common practice of fixing liability caps based on industry norms, the quantum of a liability cap should be determined by a detailed risk and liability assessment for the relevant project, and therefore it will vary from project to project. In terms of drafting, liability caps are often expressed as a percentage or a multiple of the contract price.

Determining the quantum of a liability cap will also be influenced by the extent and nature of the liability cap carve-outs. For example, the more extensive the carve-outs, the smaller the quantum of the liability cap might be. It may also be influenced by the Contractor's financial capacity to honour its liabilities, but a better way of dealing with this very important issue is to ensure the Contractor has provided appropriate security and that appropriate insurances have been taken out.

In practice, the quantum of a liability cap will be determined by reference to the Contractor's exposure. It is unlikely for the Principal to set the cap and, if it does, this will be reflected in the contract price.

Sub-caps

In addition to an overall or aggregate liability cap, sub-caps may also be used to limit liability for specific types of liability under a contract, such as the liability to pay delay liquidated damages or performance liquidated damages.

Drafting example: Liability cap and sub-caps

1. *'Subject to clauses [insert reference to the clause which excludes liability for indirect or consequential loss and the clause which specifies the carve outs to that clause and the overall liability cap], the total aggregate liability of the Contractor to the Principal under or in connection with this Contract, whether based on breach of contract or otherwise, will not exceed the Contract Price.*
2. *The aggregate liability for Delay Liquidated Damages must not exceed 10% of the Contract Price.*
3. *The aggregate liability for Performance Liquidated Damages must not exceed 10% of the Contract Price.'*

Typically, each sub-cap is mutually exclusive and applied separately to the specific liability it relates to, while the aggregate or overall cap is left to 'mop up' the other liabilities not specified in the sub-caps.

To illustrate how sub-caps might apply in practice, the application of sub-caps in relation to delay liquidated damages and performance liquidated damages is discussed in section 2.9.

Carve outs to liability caps

For a Principal, it is important that certain types of liability are excluded from an overall liability cap, as well as any sub-caps. These carve outs should align to the risks which the Contractor has assumed under the contract or assumes at law without limitation. Common carve outs to a Contractor's liability cap include liability for loss or damage in relation to:

- personal injury, disease or death
- third party property damage
- fraud, wilful misconduct, negligence or corrupt, malicious, illegal or unlawful acts
- breach of confidentiality
- breach of privacy
- claims of infringement of intellectual property
- abandonment of the works.

These carve outs are often the same as or similar to the carve outs to the exclusion of consequential loss (see section 1.4).

It is also common for Principals to carve out payments recovered or recoverable under insurances taken out in accordance with the contract. The rationale for this is that, although connected with the Contractor's liability, recovery is through the insurer rather than the Contractor, and often the cost of the insurance is borne by the Principal directly or indirectly. The drafting of an insurance carve-out needs to be done carefully to ensure it covers other payments actually recovered and payments recoverable under the insurance, in order to cover situations where the Contractor fails to comply with its insurance obligations.

1.6 Indemnities

What is an indemnity?

A contractual indemnity is a promise by one party (**indemnifier**) to pay the specified loss suffered by the other party (**indemnified**) in specified situations.[11]

Infrastructure contracts use indemnities as a means of allocating risk between the Principal and the Contractor. In particular, the Contractor often agrees to indemnify the Principal for loss in connection with:

- the Contractor's breach of the contract
- infringement of intellectual property rights licensed or assigned under the contract to the Principal
- claims for third party death, injury, illness or disease or property damage
- claims for death, injury, illness or disease to Contractor's employees.

The question as to whether an indemnity will give rise to a claim in damages or should be treated as an action for recovery of a debt has not been addressed in Australia. However, the High Court of England and Wales has specified that an indemnity gives rise to a claim in unliquidated damages.[12] The Court stated in *AXA SA v Genworth Financial Holdings Inc* 'I consider that the weight of authority, and the more orthodox view, is that a claim under a contract of indemnity is a claim in unliquidated damages'.[13]

If an indemnity is treated as a debt, it may help the claimant party to avoid dealing with some of the typical issues that may arise in claiming damages for breach of contract. For example, an indemnity can be a means to avoid grappling with the remoteness of the loss (see commentary on Hadley v Baxendale in section 1.2) and any limiting factors that may relate to the conduct of the claimant such as mitigation, contributory negligence and proportionate liability (see section 5).

Law on indemnities in Australia

Andar Transport v Brambles Limited Andar Transport Pty Ltd v Brambles Ltd [14] is a leading authority in Australia. The majority of the High Court held that an indemnity provision in a commercial contract is to be construed strictly in the context of the contract as a whole, and in the event of ambiguity, to be read *contra proferentem* in favour of the indemnifier.[15]

Similarly, in *Erect Safe Scaffolding (Aust) Pty Ltd v Sutton*,[16] Giles JA stated that '[d]ecisions on the operation of contractual indemnities in different words in different contracts are likely to be of limited assistance'.

In *Woolworths Group Ltd v Twentieth Super Pace Nominees Pty Ltd atf the Byrns Smith Unit Trust t/as SCT Logistics*, the Court found that by virtue of the construction of the contract, Woolworths was entitled to be indemnified for loss or damage to goods despite whether the loss or damage was caused by a 'force majeure' event.[17]

Law on indemnities in England

In the United Kingdom, courts have typically favoured the interpretation of the ordinary and natural meaning of the terms of the contract, rather than strictly interpreting the clause according to a technical legal doctrine.[18] The scope of liability under a contractual indemnity may rely on the nature and terms of the contract. In *Total Transport Corp v Arcadia Petroleum Ltd (The Eurus)*,[19] the Court of Appeal affirmed a paragraph in Halsbury's Laws of England stating that the 'extent of a person's liability under an indemnity depends on the nature and terms of the contract'.

In *Gwynt y Môr OFTO Ltd v Gwynt y Môr Offshore Wind Farm Ltd*,[20] the High Court of England and Wales found that the indemnity clause in question was to be construed according to the natural and ordinary meaning of the language and to reflect the intentions of the parties.

Difference between an indemnity, a guarantee and a warranty

Contractual guarantees and indemnities are both obligations and both operate to protect a person against loss suffered.[21] However, the way in which they achieve this differs.

As described above, an indemnity is a contractual promise by the indemnifier to compensate the indemnified in certain circumstances.[22] The indemnifier assumes a primary liability for the unliquidated loss.

This differs from a guarantee, which is a promise to answer for the debt or default of another who is, or may become, liable to the person to whom the guarantee is given.[23] The guarantor assumes a secondary liability which only arises if a third party (primary obligor) does not perform their obligation.[24]

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11 *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245; *Yeoman Credit Ltd v Latter* [1961] 2 All ER 294; *Total Oil Products (Aust) Pty Ltd v Robinson* [1970] 1 NSWR 701 at 703.

12 *Firma C-Trade SA v Newcastle Protection and Indemnity Association (The Fanti) (No 2)* [1991] 2 AC 1 (HL).

13 [2019] EWHC 3376 (Comm) at [117].

14 (2004) 217 CLR 424.

15 See *Coghlan v S H Lock (Australia) Ltd* (1987) 8 NSWLR 88 at 92; 70 ALR 1 at 5; *BI (Contracting) Pty Ltd v AW Baulderstone Holdings Pty Ltd* [2007] NSWCA 173 at [19] and [25]; *Rava v Logan Wines Pty Ltd* [2007] NSWCA 62 at [55]; *Cherry v Steele-Park* (2017) 96 NSWLR 548 at [112].

16 (2008) 72 NSWLR 1 at 4.

17 [2021] NSWSC 344.

18 *AXA SA v Genworth Financial Holdings Inc* [2019] EWHC 3376; *Total Transport Corp -v- Arcadia Petroleum Ltd (The Eurus)* [1998] 1 Lloyd's Rep. 351.

19 [1998] 1 Lloyd's Rep. 351.

20 [2020] EWHC 850 (Comm).

21 *Andar Transport Pty Ltd v Brambles Ltd* (2004) 217 CLR 424.

22 *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245 at 254.

23 *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245 at 254; *Re Conley (t/as Caplan & Conley)* [1938] 2 All ER 127 at 130-31; *Yeoman Credit Ltd v Latter* [1961] 2 All ER 294; *Total Oil Products (Aust) Pty Ltd v Robinson* [1970] 1 NSWR 701 at 703.

24 For example, *Turner Manufacturing Co Pty Ltd v Senes* [1964] NSWR 692; *Permanent Trustee Co of New South Wales Ltd v Hinks* (1934) 34 SR (NSW) 130.

Courts have therefore distinguished between a guarantee and an indemnity by emphasising the difference between the guarantor's secondary liability and the indemnifier's primary liability.[25] The reference to primary liability is thought to refer to ultimate liability.[26]

A warranty may be used for several different purposes:

- as a contractual warranty, being a minor term of a contract as opposed to a fundamental condition in a contract[27]
- as a representation or statement of fact made by the warrantor to the warrantee
- as to a performance level in a contract, prescribing a certain standard in relation to a good or service being provided
- as a statutory warranty in the context of consumer protection legislation.

Like indemnities, warranties are commonly used in infrastructure contracts as a means to transfer risk from one party to another and, depending upon the nature of the warranty, to enable specific remedies. If a party breaches a mere contractual warranty, the other party will not necessarily be entitled to terminate the contract or accept repudiation and recover damages, and will only be entitled to recover damages.

Drafting considerations

Both warranties and indemnities are construed strictly and any ambiguity will normally be resolved in favour of the indemnifier.[28] For example, indemnities that purport to cover the Indemnified's own negligence may be interpreted by a court on the basis that the Indemnifier did not intend this, and therefore the indemnity should be read down or limited in its scope to exclude loss caused through the Indemnified's own negligence.[29]

In *Andar Transport Pty Ltd v Brambles Ltd*, the High Court held that the requirement to construe indemnities strictly meant that certain ambiguous clauses in the contract should be read down in favour of the party providing the indemnity.[30] Similarly, in *Samways v Workcover Queensland*,[31] Applegarth J held that the phrase 'arising out of' is wide and can lead to ambiguity.

It is critical therefore that the warranties and indemnities are drafted clearly and unambiguously so as to avoid them being read down or ruled void for uncertainty.

Given the drafting complexity of indemnities (and their frequent length and detail), it is especially important to ensure the key elements of an indemnity clause are all addressed, namely:

- the party providing the indemnity
- is the party being indemnified, noting that sometimes this will include more than just the Principal itself
- the scope of the 'loss' being indemnified – a typical formulation is 'costs, expenses, loss and damage' but are those words separately defined and do they include consequential or indirect losses?
- the specified circumstances triggering the indemnity – for example, claims by third parties for death or injury
- any limits on the liability to indemnify or 'carve-outs' – for example, the Principal's own default or negligence.

It is also worth considering how any liability caps will operate on the Contractor's liability under the indemnities. If a liability cap is drafted to include liability under an indemnity, this will reduce the potency of the indemnity.

Drafting example: Scope of loss covered by an indemnity

'Each indemnity given by the Contractor in this Contract is a continuing obligation separate and independent from any other obligations. All indemnities given by the Contractor in this Contract are subject to, and limited by, the exclusion of Consequential Loss in GC [ ] and the Total Limit of Liability in GC [ ]. For clarity, no Consequential Loss will be recoverable under the indemnity in GC [ ].'

The example drafting set out below can be used where the Contractor is indemnifying the Principal for loss arising out of the Contractor's breach.

Drafting example: Indemnity in relation to breach

'The Contractor indemnifies the Principal against any Loss or Claim suffered or incurred by the Principal as a consequence of or in connection with any breach by the Contractor of the Project Agreements, save that the Contractor's liability will be reduced to the extent the Contractor demonstrates that the Loss or Claim was caused by the negligence or breach of the relevant Project Agreement by the Principal.'

The example drafting set out below can be used where the Contractor, as the assignor of intellectual property rights being licensed or assigned under the contract, is indemnifying the Principal if the intellectual property ultimately infringes a third party's intellectual property rights.

25 For example, the comments of Lord Esher MR, in Baynton v Morgan (1888) 22 QBD 74 at 77–8.

26 *Sunbird Plaza Pty Ltd v Maloney (1988)* 166 CLR 245.

27 *Tramways Advertising Pty Ltd v Luna Park* (N.S.W) Ltd (1938) (SR) (NSW) 632.

28 *Andar Transport Pty Ltd v Brambles Ltd* (2004) 217 CLR 424 at [17] – [23].

29 *Davis v Commissioner for Main Roads* (1968) 117 CLR 529 at 534 per Kitto J (Windeyer J agreeing); *Westina Corporation Pty Ltd v BGC Contracting Pty Ltd* [2009] WASCA 213 at [64] – [65].

30 *Andar Transport Pty Ltd v Brambles Ltd* (2004) 217 CLR 424 at [29].

31 [2010] QSC 127.

Drafting example: Warranty and indemnity clause in respect of intellectual property

'Intellectual Property indemnity

The Contractor indemnifies the Principal, the Principal's Representative, and its Personnel, successors and assigns or any other person with a right to use the Contractor IP or Project IP under GCs [ ] and [ ] (Indemnified Persons), from and against all Claims and Losses (including but not limited to legal costs on an indemnity basis) in any way in connection with:

- *any Claim that the Project IP or the Contractor IP or any use, reproduction, modification or adaptation by or on behalf of the Indemnified Persons infringes the Intellectual Property, moral rights or any other rights of any third party or entitles any third party to Claim any compensation, royalty fee or other amount (including, without limitation, any Loss suffered by the Indemnified Persons where any Indemnified Persons are the author of any Project IP or the Contractor IP)*
- *any breach by the Contractor of the warranties in GCs [ ] or [ ].*

If an action is brought against the Principal claiming that its use of the Spare Parts or the Licensed Technology infringes any Intellectual Property (an Infringement), the Contractor or its Affiliates have the right and obligation to defend the Principal at the Contractor's expense and the Contractor has sole control over the defence of the claim and any negotiation for its settlement but must use its best endeavours to ensure that any defence or settlement provides that the Principal can continue to operate the [infrastructure project] in accordance with the terms of this Contract. The Contractor shall indemnify the Principal in connection with any direct loss (and any loss described in GC [ ]) specifically on account of such infringement or as agreed by the Contractor in an out of court settlement but only if:

- *the Principal notifies the Contractor of the Infringement*
- *the Principal takes no negligent or wilfully wrongful action that impairs the Contractor's defence of the claim*
- *the Principal acts in accordance with the Contractor's reasonable instructions.*

At the Contractor's request, the Principal shall cooperate with the Contractor in such defence.

The Contractor must not settle any action referred to in GC [ ] without the prior written consent of the Principal if by such settlement the Principal is obliged to suffer any loss, to make any monetary payment, to part with any property or any property interest, to assume any obligations or to grant any licence or other rights (to the extent that the Principal is not indemnified in accordance with GC [ ]).

Moral rights

The Contractor warrants that the performance of the Works, the provision of the Project IP or Contractor IP to the Principal and the use of the Project IP or the Contractor IP by the Principal or its licensees and sublicensees (including making distortions, additions or alterations to the Project IP and the Contractor IP) will not:

- *require the Principal or its licensees and sublicensees to identify the authority of any such work, or*
- *infringe or contravene any moral rights or similar personal rights which by law are not assignable, of any person,*

and all necessary consents to give effect to this warranty have been or will be obtained, and will be effective and irrevocable.'

Other drafting considerations

It is also important to consider whether the indemnity drafting should set out the machinery for the making of a claim and the payment of or recovery of the indemnity, including any requirements in relation to notices to be given, the timing of the payment and any rights of set off.

Drafting example

'Conduct of Claims

As soon as reasonably practicable after the Contractor receives any Claim or demand or is served with any legal proceedings which is likely to lead to liability on the part of the Principal under any Claim, the Contractor must give written notice to the Principal setting out details of the Claim, demand or legal proceedings.

The Contractor must not compromise or pay any Claim or demand or admit liability in relation to any Claim or demand or agree to arbitrate, compromise or settle any legal proceedings which is likely to lead to liability on the part of the Principal under any Claim without the prior written approval of the Principal (such approval not to be unreasonably withheld or delayed).

Subject to clause [ ], in respect of a Claim for which the Principal has accepted liability, the Principal may at any time at its election:

- *require the Contractor (and the Contractor must) at the cost of the Principal to take such action as the Principal reasonably requires to avoid, contest, compromise or defend any Claim, demand or legal proceedings which may lead to liability on the part of the Principal under such Claim, or*
- *take over responsibility for the conduct or defence of such Claim or demand or legal proceedings at the cost of the Principal and the Contractor must cooperate with the Principal in such circumstances.*

The Contractor is not required to take any action or conduct or defend any Claim or demand or legal proceedings in accordance with clause [ ] if to do so would be detrimental to the ongoing conduct of the Contractor's Business.'



2
Liquidated damages

2.1 Introduction

Liquidated damages are an efficient, accessible and convenient contractual remedy for specified breaches of contract. In infrastructure contracts, they are commonly used as a Principal remedy for Contractor breaches in relation to the delayed completion or underperformance of works.

A liquidated damages regime operates in the following way:

- At the time of entering into the contract, the parties agree to fix (for example, liquidate) the actual amount payable as damages in respect of breach of a specific obligation by the Contractor.
- If a breach of that obligation occurs, the Principal's right to claim liquidated damages arises and the pre-agreed liquidated damages are payable by the Contractor or set off against payments due to the Contractor, without the Principal needing to prove actual loss.
- In some circumstances, this may prove to be a windfall for the Principal if its actual loss suffered is less than the liquidated damages. In other cases, the liquidated damages may be less than the actual loss suffered by the Principal. In the former case, the Contractor is unable to complain unless it seeks to challenge the enforceability of the liquidated damages regime itself (for example because the liquidated damages amount constitutes a 'penalty' – see discussion below). In the latter case, the Principal is unable to seek further damages from the Contractor as the pre-agreed liquidated damages are in effect treated as a 'cap' on the Contractor's liability for the relevant breach.

Two common types of liquidated damages are 'delay liquidated damages' and 'performance liquidated damages'. These are discussed in turn in sections 2.2 and 2.3.

2.2 Delay liquidated damages

Delay liquidated damages are payable by the Contractor to the Principal if the works are not completed by the fixed date for completion. Their purpose is to compensate the Principal for the losses it will suffer as a result of the delay. These losses may include direct and indirect losses, for example, additional costs incurred in relation insurances required, corporate overhead, increased supervision and other consultancy fees, financing charges and revenue forgone.

Delay liquidated damages are typically expressed as a rate payable for each day, week or month of the delay to the completion of the works. This is a way of ensuring that the liquidated damages payable will accurately reflect the actual losses that will be suffered for the relevant period of delay.

Example delay liquidated damages regime

An example delay liquidated damages regime is set out below.

Drafting example: Delay liquidated damages regime

1. *'If the Contractor does not achieve Commercial Operation by the Date for Commercial Operation, the Contractor must pay the Principal the following Delay Liquidated Damages:*
    a. *[insert amount] per day of delay*
    b. *if the Commercial Operation Date does not occur by the specified dates below (such that the Principal incurs [insert a description of specific additional costs that the Principal will incur, for example, because it will be in breach of an offtake agreement if Commercial Operation is not achieved by a certain date]):*
        i. *[insert date] – [insert amount]*
        ii. *[insert date] – [insert amount]*
2. *The total revenue (if any) received by the Principal from any sale of [insert output of facility, for example, electricity] before the Commercial Operation Date but after the Date for Commercial Operation, will be offset from the amounts payable under clause 1.'*

2.3 Performance liquidated damages

Performance liquidated damages are discussed in further detail in Annexure A.

Performance liquidated damages are payable by the Contractor to the Principal if the works (for example, a facility) underperform. Their purpose is to compensate the Principal for the losses it will suffer as a result of the underperformance of the facility. These losses may include direct and indirect losses, for example, revenue forgone as a result of the reduced output.

The nature of performance liquidated damages will depend on the performance guarantee(s) provided by the Contractor for the facility — that is, the agreed performance specifications that the facility must achieve, as measured in terms of, for example, efficiency, output or availability.

Performance liquidated damages are typically expressed as a net present value calculation of the revenue forgone over the design life of the facility. For example, in the case of a power solar PV facility, if the output of the facility is 5 MW less than the performance guarantee, the performance liquidated damages will equal the revenue forgone over the life of the facility as a result of being unable to sell that 5 MW shortfall.

'Performance guarantees' vs 'minimum performance guarantees'

Some performance liquidated damage regimes have a two tier structure which provides that after certain minimum performance guarantees are met, the Principal will assume care, custody and control of the facility but continue to allow the Contractor to work on the facility and attempt to improve its performance while continuing to pay delay liquidated damages.

This regime is appropriate where:

- the Principal prefers to take possession of the facility and begin operations as soon as commercial operation is achieved (effectively, in certain circumstances, as soon as the minimum performance guarantees are met)
- it is viable, even after the Principal has assumed the care, custody and control of the facility, for the Principal to allow the Contractor access to attempt to improve performance while continuing to pay delay liquidated damages.

2.4 Drafting an enforceable liquidated damages clause

The enforceability of a party's right to liquidated damages will be assessed by reference to the common law penalties doctrine. This is on the basis that a liquidated damages regime, in accordance with the first limb of that doctrine, imposes a detriment as a collateral or secondary obligation (being the obligation to pay liquidated damages). This arises upon a breach of a primary obligation (being the obligation, for example, to complete the works by a fixed date for completion or in compliance with various performance guarantees).[32]

The concern for Principals is the second limb of the penalties doctrine. It historically provided that a liquidated damages clause will be unenforceable if the amount set as liquidated damages is not a 'genuine pre-estimate of the damage' that would be suffered in the relevant circumstances. However, as discussed below, recent case law has reframed this second limb in terms of the 'legitimate interests' of the parties.

In accordance with the case law below, the question of whether a liquidated damages regime constitutes a penalty is one of construction to be decided upon the terms and circumstances of each particular contract at the time of formation. Whether a clause uses the words 'penalty' or 'liquidated damages' is not conclusive of its enforceability.[33]

If the liquidated damages are found to be a penalty, they will be unenforceable under common law. However, the Principal will still be able to recover unliquidated damages at law provided the contract does not contain an exclusive remedies clause (see discussion in section 2.6).

The penalties doctrine under English law

The penalties doctrine was most recently considered by the Supreme Court of the United Kingdom in the case of *Cavendish Square Holding BV v Talal El Makdessi; ParkingEye Limited v Beavis* [2015] UKSC 67 (**Cavendish**).

In this case, the majority moved away from the concept of 'genuine pre-estimate of damage', instead reframing the test as whether a liquidated damages clause 'imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation'.[34] If found to do so, it will be deemed a penalty and therefore unenforceable.

Therefore, the new question for a Principal is — what constitutes its legitimate interests? Here, the majority of the Supreme Court made it clear that the considerations which may be taken into account are broad. For example, it was recognised that compensation is not necessarily the only legitimate interest that a party may have.[35] Further, the majority also noted that where a liquidated damages regime is negotiated between properly advised parties of comparable bargaining power, the 'strong initial presumption must be that the parties themselves are the best judges of what is legitimate'.[36]

The penalties doctrine under Australian law

Shortly after the Cavendish decision was handed down, the High Court of Australia also had the opportunity to reconsider the penalties doctrine in the case of *Paciocco v Australia and New Zealand Banking Group Limited* (2016) 258 CLR 525.

In this case, the majority closely followed the Cavendish decision and similarly reframed the penalties doctrine, holding that a liquidated damages clause will be unenforceable if it is 'out of all proportion' with the 'legitimate interests' of the party it serves to protect.[37] The majority also emphasised, as in Cavendish, that few constraints apply to the scope of the 'legitimate interests' concept.

32 *Andrews v Australia and New Zealand Banking Group Limited* (2012) 247 CLR 205, [10]; *Cavendish Square Holding BV/Beavis v Talal El Makdessi/ParkingEye Limited* [2015] UKSC 67, [14]-[15] (Lord Neuberger and Lord Sumption, Lord Carnwath and Lord Clarke agreeing).

33 Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd [1915] AC 79, [86] (Lord Dunedin).

34 *Cavendish Square Holding BV/Beavis v Talal El Makdessi/ParkingEye Limited* [2015] UKSC 67, [32] (Lord Neuberger and Lord Sumption, Lord Carnwath and Lord Clarke agreeing).

35 Ibid.

36 Ibid, [35] (Lord Neuberger and Lord Sumption, Lord Carnwath and Lord Clarke agreeing).

37 *Paciocco v Australia and New Zealand Banking Group Limited* (2016) 258 CLR 525, [51]-[56] (Kiefel J, French CJ agreeing at [2]), [166] (Gageler J), [269]-[270] (Keane J).

However, unlike in Cavendish, the majority did not completely discard with the 'genuine pre-estimate of damage' formulation. Instead, it appears that it will remain as a form of catchphrase, but with the new 'legitimate interest' test adopted as the proper methodology for determining what is considered enforceable. Indeed, as the majority accepted, the exercise of pre-estimating losses may be difficult and 'not one which calls for precision'.[38]

Also unlike in Cavendish, the majority refrained from any meaningful discussion about whether discretionary factors such as the relative bargaining power of the parties would be considered in assessing the legitimacy of a liquidated damages clause.

Distinguishing between delay liquidated damages and performance liquidated damages

We have seen infrastructure contracts where delay liquidated damages and performance liquidated damages are combined, that is, the same liquidated damages are payable by the Contractor both when the works are delayed or when they fail to meet the performance guarantees.

This drafting approach is not recommended. A combined liquidated damages regime may not differentiate between the different types of breaches and their corresponding losses. For example, it may not differentiate between the alternate scenarios where (a) the works are delayed only but otherwise meets all performance guarantees, or (b) where the works fail to meet the performance guarantees but otherwise were completed on time. In both these circumstances, the liquidated damages ostensibly include a category of loss which the Principal has not suffered. It creates a high risk that the liquidated damages regime will be struck down as a penalty on the basis that it is out of all proportion to the legitimate interests of the Principal when only one type of breach occurs.

Distinguishing between different types/categories of performance liquidated damages

It is also important distinguish between different types/categories of performance liquidated damages to avoid any potential challenges by the Contractor that the performance liquidated damages are out of all proportion to the legitimate interests they serve to protect.

For example, if performance liquidated damages are calculated by reference to output but not efficiency, challenges and uncertainties may arise if a facility meets the specified output guarantees but fails to meet the specified efficiency guarantee. In these circumstances, the Contractor may argue first, that the (output based) performance liquidated damages do not apply and second, if they do apply, that they constitute a penalty because they reflect losses that would be suffered for output shortfalls which are higher than losses that would be suffered for efficiency underperformance.

A combined performance liquidated damages regime is unlikely to be the answer for the same reasons why combined delay liquidated damages and performance liquidated damages are inherently problematic, as discussed above.

2.5 Liability caps in relation to liquidated damages

In practice, the liquidated damages amounts set for major infrastructure projects that are financed on a non-recourse or limited recourse basis are typically estimated below the likely loss that a Principal would suffer. This reflects the commercial reality that the market will only bear a certain level of liquidated damages, and the acceptance of that reality by the Principal given the market response and the significant advantages to it of a liquidated damages regime.

In addition, most infrastructure contracts contain an overall cap on the Contractor's liability for liquidated damages, often expressed as a percentage of the contract price. There may also be sub-caps for each of delay liquidated damages and performance liquidated damages.

As with all liability caps, this has the effect of transferring the relevant delay and/or performance risk to the Principal. One approach for Principals to deal with this risk is to include a right to terminate when the liquidated damages cap is reached.

2.6 Losing the right to delay liquidated damages if Principal causes delay

Even if a contract contains an enforceable delay liquidated damages regime, the Principal will lose its right to claim delay liquidated damages if it prevents the completion of the works and the Contractor is not given an extension of time to the fixed date for completion. This is the 'prevention principle' at work, discussed further in section 4.

Indeed, it is quite common for Contractors to claim that the Principal has committed an act of prevention, especially when an event occurs that is not expressly contemplated by the contract and not within the Contractor's sphere of responsibility.

This means it is imperative for infrastructure contracts to have a comprehensive extension of time regime that allows extensions to be granted in all circumstances where the delay to the fixed date for completion is caused by a Principal act of prevention.

The 'prevention principle' and the corresponding risk it has for the liquidated damages regime also highlights the importance of the Principal resisting the inclusion of an exclusive remedies clauses (discussed in section 2.7).

2.7 Are liquidated damages the Principal's only remedy?

If a liquidated damages regime is found to be unenforceable (for example because it constitutes a 'penalty' — see section 2.4), the Principal may still claim damages at law in respect of its loss, provided there is no exclusive remedies clause which would prevent this or exclude such a right.

38 Ibid, [57]-[58] (Kiefel J, French CJ agreeing at [2]), [176] (Gageler J), [243] (Keane J).

However, if a contract contains an exclusive remedies clause, the Principal may be prevented from doing so — where that exclusive remedies clause provides that the remedies expressly provided for in a contract (for example, liquidated damages) are to the exclusion of any remedies at law. In these circumstances, a Principal may be left without any monetary compensation for delay or underperformance. Depending on the drafting of the exclusive remedies clause however, it may still be open to the Principal to call on other express remedies such as termination.

Exclusive remedies clauses are discussed further in section 3.

2.8 Failsafe clauses to ensure remedies at law remain available

If a liquidated damages regime is found to be unenforceable because it constitutes a 'penalty' (see section 2.4) or because the Principal commits an act of prevention (see section 2.5), a failsafe clause may preserve the Principal's right to obtain a remedy at law.

An example failsafe clause in relation to a delay liquidated damages regime is set out below.

Drafting example: Failsafe clause in relation to a delay liquidated damages regime

'If this clause (or any part thereof) is found for any reason to be void, invalid or otherwise inoperative so as to disentitle the Principal from claiming "Delay Liquidated Damages", the Principal is entitled to claim damages at law against the Contractor for its failure to achieve "Completion" by the "Date for Completion" up to the "Aggregate Liability Cap for Delay Liquidated Damages".'

Contractors often argue that an exclusive remedies clause should be included in its contract without a failsafe clause so that liquidated damages are the Principal's only possible remedy for the Contractor's delay or underperformance. As discussed in section 3.6, we advise that Principals should resist this.

2.9 When are delay liquidated damages and performance liquidated damages paid?

It is common for a liquidated damage regime to operate in the following way (assuming neither the Principal or the Contractor exercises any right to terminate the contract):

- Delay liquidated damages are payable by the Contractor if the facility is not completed by the agreed date for completion. These are invoiced by the Principal in accordance with the agreed calculation, for example a rate payable for each day, week or month of the delay.
- The Contractor's aggregate liability for delay liquidated damages will be subject to a liability sub-cap (for example 10% of the contract price).
- Performance liquidated damages are payable by the Contractor if the facility does not meet the performance guarantees at the agreed date for completion and one of the following occurs:
  - the Principal determines or the Contractor elects at any time after that date that the Contractor will stop further modifications of the facility
  - the Contractor's liability for delay liquidated damages has been exhausted under the sub-cap for delay liquidated damages (for example, the cap has been reached).

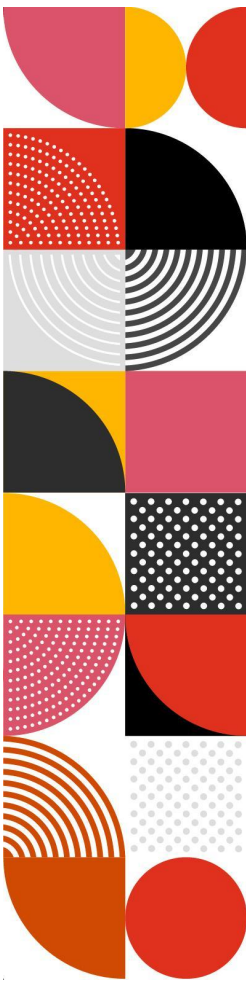
What if there is also an availability guarantee?

The simplified liquidated damages regime above does not take into account that performance liquidated damages may also arise because a facility fails to meet an availability guarantee. This is because performance against an availability guarantee is measured over a period of time.

An example availability guarantee is set out below.

Drafting example: Availability guarantee

'The Contractor guarantees that the facility will operate at the guaranteed availability for a period of 12 months from not later than two months after the Date of Commercial Operation.'



3
Exclusive remedy clauses

3.1 Introduction

Contractors commonly request a clause which provides that the remedies expressly provided for in a contract (for example termination, suspension, force majeure and liquidated damages) are to the exclusion of any remedies at law (**exclusive remedies clause**). In the same vein, they may also request to remove any express references to a Principal's recourse to remedies at law.

Contractors have a number of reasons for doing this, including:

- increasing the certainty of their agreements by specifying the remedies they agree to
- fixing their financial exposure in the event of any breach, delay or non-performance
- being able to expedite dispute resolution processes by making it clear that only remedies expressly provided for in the contract can be called on.

Agreeing to an exclusive remedies clause may have significant consequences for a Principal. In particular, it will limit their legal remedies to those expressly set out in the contract and, in some cases where there are no remedies for a particular liability, it will leave the Principal without a remedy at all.

The true effect of an exclusive remedies clause will always depend on its drafting. The key issues to be determined are:

- What remedies at law are being excluded? Is it all remedies or only common law damages?
- In respect of which legal liabilities are the remedies at law being excluded? Is it all types of legal liability, including negligence and breach of contract, or only particular liabilities such as the liability to pay liquidated damages?

If a contract does not contain an exclusive remedies clause, a Principal may be able to claim remedies at law (for example, breach of contract) as an alternative to any remedies expressly provided for in the contract (for example, liquidated damages), including in circumstances where the relevant contractual remedy is held to be unenforceable (see discussion in section 2.6 in relation to liquidated damages).

3.2 Exclusive remedies clauses

An exclusive remedies clause attempts to prevent a Principal from seeking common law remedies, including damages, as an alternative or in addition to the remedies expressly provided for in a contract (for example, liquidated damages), including where the express contractual remedy is unenforceable.

An example exclusive remedies clause is set out below.

Drafting example: Exclusive remedies clause

'The parties agree that their respective rights, obligations and liabilities as provided for in this Contract are exhaustive of the rights, obligations and liabilities of each of them to the other arising out of, under or in connection with this Contract or the Works, whether such rights, obligations and liabilities arise in respect or in consequence of a breach of contract, a statutory duty or a tortious or negligent act or omission which gives rise to a remedy at common law. Accordingly, except as expressly provided for in this Contract, neither party will be obligated or liable to the other in respect of any damages or losses suffered by the other which arise out of, under or in connection with this Contract or the Works, whether by reason or in consequence of any breach of contract, a statutory duty or tortious or negligent act or omission.'

The above example clause would significantly affect a Principal's ability to recover any losses it suffers. In particular, the final sentence provides that, other than those clauses in the contract for which a remedy is specifically provided, the Principal is not able to recover its loss from the Contractor arising out its breach of contract, breach of statutory duty or any tortious or negligent act or omission. It follows that, if there has been a failure by the Contractor to satisfy a contractual obligation, or if the Contractor has been negligent, then unless the Principal can point to a remedy expressly provided under the contract for such a breach or negligence, it would be left without a remedy.

3.3 Could a liquidated damages regime be sufficient?

Although a contract might include a delay liquidated damages regime and a performance liquidated damages regime, the Principal is usually concerned about more than just meeting the date for completion and performance guarantees.

There are many other Contractor obligations under a contract for which remedies should be available in the event of non-compliance or breach. If a comprehensive exclusive remedies clause is inserted and no remedy has been expressly provided for in the contract, then there are no legal consequences for these failures of the Contractor, no rights of the Principal to recover its loss and a resulting transfer of liability risk from the Contractor to the Principal.

3.4 Enforcing exclusive remedies clauses

It is clear that, whether the terms of a contract constitute a full statement of the rights and liabilities of the parties so as to exclude remedies at law, depends on the construction of each individual contract.[39] If a party's right at law to claim a remedy for a breach of contract is to be removed contractually, it must be done by clear words.[40]

Courts in both England and Australia have held that clear wording may remove the common law right to damages. This view has been followed in a number of cases.[41] In *Baese Pty Ltd v RA Bracken Building Pty Ltd* (1990) 6 BCL 137, Giles J stated at 142 that:

> *[…] it would require clear words […] before it was held that a liquidated damages clause was the entirety of the proprietor's rights, because the proprietor would be exposed to being left with no entitlement at all to damages for delay if by reason of his own contribution thereto he was unable to rely upon the liquidated damages clause.*

This position has arguably been broadened by Australian courts, so that 'clear words' does not necessarily mean 'express words'. In *Turner Corporation Ltd (Receiver and Manager Appointed) v Austotel Pty Ltd*,[42] Cole J at 36 held that a party's rights to common law damages do not need to be excluded by express words, rather, a general intention, surmised from the terms of the contract more generally, can be sufficient:

> *If on the proper construction of the contract as a whole, it can be said that a party has surrendered its common law rights to damages, that construction must be given effect to, notwithstanding absence of express words surrendering the common law rights to damages.*

However, the identification of one remedy in a contract is not in itself enough to impliedly exclude other remedies.[43]

This is an important and controversial statement of principle, as it suggests that if, on the structure of the contract as a whole, it appears that a party has surrendered its rights to common law damages by the insertion of a particularly comprehensive exclusive remedies clause, that party will have no remedies other than those specifically stated in the contract.

3.5 Enforcing exclusive remedy clauses

Generally speaking, when in interpreting a contract, a court will aim to give effect to the parties' intentions as evidenced from the terms of the contract. Therefore, where the parties have expressly provided that the remedy set out in the contract (for example, liquidated damages) is to be an exclusive remedy, the courts will not interfere with this position. However, it is also clear from the authorities referred to above that, if a party's right at law to claim remedies for a breach of contract is to be contractually removed by an exclusive remedy clause, this must be done by clear words.

That said, courts have upheld less clearly worded exclusive remedy clauses.

For example, in *Temloc Ltd v Errill Properties Ltd* (1987) 39 BLR 30, a clause in a contract appeared under the heading 'Damages for Non-Completion' and stated that the amount of 'liquidated and ascertained damages' to be paid was as stated in the Appendix. The relevant section in the Appendix was completed with the word 'nil'. The court held that, on the proper construction of the contract, the parties had come to an exhaustive agreement that no damages would be payable by the Contractor at all for delayed completion, including no unliquidated damages at law.

3.6 Recommended solutions

A Principal's preferred position must always be to resist surrendering any legal rights, and therefore it should reject a proposal to include an exclusive remedies clause in a contract.

If that is not possible, there may be other compromise options available. One such option is for a Principal to accept a carefully drafted exclusive remedies clause which:

- is limited to a specific breach (for example, delay) and for which there is an express remedy in the form of delay liquidated damages
- only excludes specific remedies at law such as damages or other forms of monetary compensation, but does not exclude other rights, such as the right to terminate the contract.

39 *Turner Corporation Ltd (Receiver & Manager Appointed) v Austotel Pty Ltd* (1994) 13 BCL 378.

40 *Bitannia Pty Ltd v Parkline Constructions Pty Ltd* (2010) 26 BCL 335 at [77]; *Concut Pty Ltd v Worrell* (2000) 75 ALJR 312 at [23]; *H W Nevill (Sunblest) v William Press & Sun* (1981) 20 BLR 78, 88; *Baese Pty Ltd v R A Bracken* (1990) 6 BCL 137.

41 For example, *Photo Production Ltd v Securicor Transport Ltd [1980] AC 827 (Lord Diplock); Hancock v Brazier (Anerley) Limited (1966) 1 WLR 1317; Billyack v Leyland Construction Co Ltd (1968) 1 WLR 471; Bitannia Pty Ltd v Parkline Constructions Pty Ltd (2010) 26 BCL 335 at [77]; Concut Pty Ltd v Worrell* (2000) 75 ALJR 312 at [23]*; H W Nevill (Sunblest) v William Press & Sun (1981) 20 BLR 78; Baese Pty Ltd v RA Bracken Building Pty Ltd (1990) 6 BCL 137.*

42 (1994) 13 BCL 378.

43 *Semantic Software Asia Pacific Ltd v Ebbsfleet Pty Ltd* (2018) 124 ACSR 146; *Gilbert-Ash (Northern) Ltd v Modern Engineering (Bristol) Ltd* [1974] AC 689; *Concut Pty Ltd v Worrell* (2000) 176 ALR 693.

There remains a risk with this approach which is that if the remedy expressed in the contract (for example, delay liquidated damages) is found to be unenforceable, the right to claim the specified and excluded remedies at law will have been lost, unless there is some form of failsafe clause which preserves a Principal's right to obtain remedies at law. This is discussed further in the context of liquidated damages in section 2.7.

If the Contractor insists on an exclusive remedies clause another option is to ensure that the Principal has an express remedy in the contract that corresponds to each obligation or liability of the Contractor. However, the risks associated with this approach are leaving gaps and drafting less than adequate remedies.

A modified approach might be to include a 'code of rights' provision in the contract, providing that, except where express remedies are specifically provided under the contract (for example, under a liquidated damages regime), each party will be able to claim remedies at law for breaches of the contract.

4
Prevention Principle

4.1 What is the Prevention Principle?

The 'Prevention Principle' is classically applied by the courts in infrastructure contracts to preclude Principals from claiming liquidated damages for delay in circumstances where the Principal is itself responsible for causing the delay. Sometimes known as the 'Peak' Principle, in reference to the English case of Peak Construction *(Liverpool) Ltd v McKinney Foundations Ltd* (1970) 1 BLR 111 (**Peak**) where the principle was first applied, the Prevention Principle ensures that neither party may benefit under the contract from its own breach.

The position under English law is that if the Principal prevents the completion of the works in any way, it loses the right to claim liquidated damages for failure to complete by the fixed date for completion.[44]

Acts of prevention resulting in the loss of the right to levy liquidated damages typically include breach of express and implied obligations under the contract. However, they also extend to acts that are in accordance with the contract but that prevent completion by the date for completion, for example, ordering extras as a variation, and the Prevention Principle can apply even where the Contractor is also responsible for part of the delay. We examine the broad application of the rule in more detail below.

The Prevention Principle has also been applied in the same way in Australia as it has in England.[45] In fact, acts of prevention were extended significantly by the court in *Peninsula Balmain Pty Ltd v Abigroup Contractors Pty Ltd* (2002) 18 BCL 322. In that case, the Contractor failed to comply with the prescribed notice or claim requirements under the contract. The court decided that the contract administrator was nevertheless required to consider the merit of the Contractor's claim honestly and fairly, and if it did not do so, this would be an act of prevention.

4.2 The operation of the Prevention Principle

Time at large

Under infrastructure contracts, the effect of the Prevention Principle is that if the Principal causes delay to the date for completion and there is no extension to the date for completion, time will be considered to be 'at large', meaning that the Contractor has a reasonable time within which to complete. There no longer being an ascertainable date for completion, the Principal cannot levy liquidated damages and the remedy is lost.

The loss of the right to levy liquidated damages is more acute for the Principal if the contract also contains an exclusive remedies clause that precludes recovery of common law damages. What this means is that if time is 'at large' as a consequence of the Prevention Principle and the Contractor fails to complete within a reasonable time, the Principal may also be denied common law damages for the breach.

Rationale

There are various rationales for the existence of the Prevention Principle. They have been variously described as:

- the principle that a party should not be able to recover damages caused by that same party
- an implied term or implied supplemental contract[46]
- waiver or estoppels[47]
- unjust enrichment.

Others have suggested that there is in fact no coherent overarching rationale for the Prevention Principle or that it may be regarded as a manifestation of the obligation to cooperate implied as a matter of law in all contracts (see *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596, 607 (Mason J) and *Bensons Property Group Pty Ltd v Key Infrastructure Australia Pty Ltd* [2021] VSCA 69). In any case, the fundamental considerations are of fairness and reasonableness.[48]

44 *Trollope & Colls Ltd v North West Metropolitan Regional Hospital Board* [1973] 1 WLR 601 at 607; *Multiplex Ltd v Honeywell Ltd (No 2)*.

45 See, for example, *Gaymark Investments Property Ltd v Walter Construction Group (1999) 16 BCL 449* and more recently *Probuild Constructions (Aust) Pty Ltd v DDI Group Pty Ltd* (2017) 95 NSWLR 82.

46 *SBS International Pty Ltd v Venuti Nominees Pty Ltd* [2004] SASC 151, [11] (Besanko J).

47 Ibid.

48 *SMK Cabinets v Hili Modern Electrics* [1984] VR 391, 397 (Brooking J); *Spiers Earthworks Pty Ltd v Landtec Projects Corp Pty Ltd (No 2)* (2012) 287 ALR 360*; Probuild Constructions (Aust) Pty Ltd v DDI Group Pty Ltd* (2017) 95 NSWLR 82.

Response to the Prevention Principle

The Prevention Principle will not operate if the contract contains a mechanism which allows the fixed date for completion to be extended to reflect the delay to that date caused by the Principal's acts of prevention, and that mechanism is exercised.

In many infrastructure contracts there is also an 'override' clause which permits the Principal or the Contract Administrator to extend the date for completion at any time and for any reason, and whether or not the Contractor has submitted an extension of time claim. It can be used to defeat the Prevention Principle in circumstances where the extension of time clause is deficient or is not administered properly.

Neither a comprehensive extension of time mechanism nor an override clause will, however, protect the Principal from the Prevention Principle where the Principal or the Contract Administrator (as relevant) fails to invoke either of these provisions.

As discussed earlier, under both English and Australian law the scope of acts of prevention giving rise to the Prevention Principle is broad. Courts have generally regarded any wrongful act or fault as sufficient to enliven the principle, and it is not necessary that the act constitutes a breach of contract or carries any fault element.

The extension of time clause therefore needs to be drafted in similarly broad terms and if there is any ambiguity, Peak makes it clear that the clause will be construed *contra proferentem* against the Principal. Delay events described as 'events beyond the control of the Principal', do not appear to be sufficient.[49] However, where the extension of time clause provides specifically for the Principal's breach, waiver or prevention, the Prevention Principle will not apply and the liquidated damages regime will be preserved. As stated by Salmon LJ in Peak:[50]

> *'The liquidated damages and extension of time clauses in printed forms of contract must be construed strictly contra proferentem. If the Principal wishes to recover liquidated damages for failure by the Contractors to complete on time in spite of the fact that some of the delay is due to the Principals' own fault or breach of contract, then the extension of time clause should provide, expressly or by necessary inference, for an extension on account of such a fault or breach on the part of the Principal.'* [51]

One of the more contentious aspects of this area of law concerns the interaction of conditions precedent to the granting of an extension of time with the operation of the Prevention Principle. The issue is whether the Prevention Principle is subject to an administrative act (such as the provision of notice by the Contractor) or whether it can operate independently of such procedural requirements of particular contracts.

In England, Jackson J in *Multiplex Ltd v Honeywell Ltd (No 2)* held that the Prevention Principle is not engaged when the parties have agreed to make notice by the Contractor a condition precedent, as terms requiring notice of delay 'serve a valuable purpose'.[52] However, the case law in Australia remains divided. In *Gaymark v Walter Construction* (**Gaymark**),[53] the contract under dispute provided that a notice of delay was to be given within 14 days of the cause of delay arising. The Supreme Court of the Northern Territory reaffirmed an arbitral award that found that, even though the notice requirements were not complied with by the Contractor, because at least some of the delay was caused by the Principal, the right to claim liquidated damages was lost and time was set at large. This view has been subjected to strong academic criticism.[54] Later cases have suggested that conditions precedent must be satisfied before the Prevention Principle can have application. Indeed, *in Turner Corporation Limited (Receiver and Manager Appointed) v Austotel Pty Ltd*,[55] Cole J stated that the builder could not:

> *[...] claim that the act of prevention which would have entitled it to an extension of the time for practical completion resulted in its inability to complete by that time. A party to a contract cannot rely upon preventing conduct of the other party where it failed to exercise a contractual right which would have negated the affect [sic] of the preventing conduct.*[56]

A further question regarding the scope of the Prevention Principle concerns the extent to which the liquidated damages regime is invalidated by the Principal's act of prevention, and how to reset the completion date where there are concurrent delays, including as a result of a Principal act of prevention. If the Principal causes four days of delay to a Programme, and the Contractor is 100 days late in delivery of the project, can the Principal recover 96 days of liquidated damages, or is the entire liquidated damages regime invalidated? And what is considered to be a reasonable time to complete?

Early authority on this point favoured the view that any act of prevention by the Principal invalidated the entire liquidated damages regime. In *Holme v Guppy*,[57] the delay in completion was five weeks; the Principal was responsible for four weeks of the delay and the Contractor for one week. The court found that the Principal was not entitled to any liquidated damages due to its act of prevention.

This view appears to be based on the needs of certainty and predictability and finds its foundation in the classic case of Peak. More recent authority suggests that the Principal's delay and the Contractor's delay could be in some circumstances divisible for the purposes of determining and enforcing liquidated damages, but should be viewed with caution in light of Peak's authority. In *Rapid Building Group Ltd v Ealing Family Housing Association Ltd*,[58] Lloyd LJ remarked that:

49 Jones, D., 2009. Can Prevention be Cured by Time Bars?, *Society of Construction Law*, (Paper 158).

50 (1970) 1 BLR 111.

51 Ibid, 121.

52 [2007] EWHC 447 (TCC).

53 [1999] 16 BCL 449.

54 Wallace, I. D., 2002. Prevention and Liquidated Damages: A Theory Too Far?, *Building and Construction Law,* pp. 18, 82.

55 (1994) 13 BCL 378, [11] (Cole J).

56 Ibid.

57 (1838) 3 M&W 387.

58 (1984) 29 BLR 5.

I was somewhat startled to be told in the course of the argument that if any part of the delay was caused by the Owner, no matter how slight, then the liquidated damages clause […] becomes inoperative.[59]

I can well understand how that must necessarily be so in a case in which the delay is indivisible and there is a dispute as to the extent of the Owner's responsibility for that delay. But where there are, as it were, two separate and distinct periods of delay with two separate causes, and where the dispute relates only to one of those two causes, then it would seem to me just and convenient that the Owner should be able to claim liquidated damages in relation to the other period.[60]

Nevertheless, Lloyd LJ went on to note that:

[…] it was common ground before us that is not a possible view […] in the light of the decision of the Court of Appeal in Peak's case, and therefore I say no more about it.[61]

In *SMK Cabinets v Hili Modern Electrics*,[62] Brooking J stated that the Principal's act of prevention served only to prevent the Principal from taking liquidated damages that accrued after the Principal's breach.[63] While this view has much to commend it, the case of Peak remains dominant and authorities seem to suggest that where an act of prevention goes to part of the delay but not the whole, the entire liquidated damages clause will be invalidated. This traditional view has been reinforced in Australia *in SBS International Pty Ltd v Venuti Nominees Pty Ltd*,[64] where Besanko J held that, in a situation where delay to the completion date is caused by the Contractor as well as the Principal, it is not open to a court to apply the liquidated damages clause to the delay specifically caused by the Contractor:

In those cases where both Principal and Contractor are responsible for delay, the liquidated damages clause will be held inapplicable unless there is a contractual provision by way of an appropriate extension of time clause which accommodates or deals with the delay caused by the contract of the Principal.[65]

There is some uncertainty as to the application of the Prevention Principle in the context of offshore shipbuilding contracts. Hamblen J in *Adyard Abu Dhabi v SD Marine Services* [2011] EWHC 848 (Comm) confirmed that the Prevention Principle applies to shipbuilding contracts generally, but later shipbuilding cases have avoided detailed discussion on the Prevention Principle.[66] As such, where the contract is seen as a complete code setting out the intention of the parties as to the allocation of the risk of delay, if the Contractor is delayed by anything that is not a permissible delay under the contract, it is considered to be a Contractor's risk.

4.3 Can the Prevention Principle be contracted out of?

It is possible for the parties to provide that some acts of prevention escape the Prevention Principle. However, this would need to be done by very careful drafting, given the presumption that the parties do not intend for the Contractor to take on the risk of the Principal's acts of prevention. One example of seeking to narrow the scope of the Prevention Principle and paring back the corresponding extension of time clause is set out below.

Drafting example

Set out below is an example definition of 'Act of Prevention':

'Act of Prevention means:

- *any act by the Principal or its Personnel, other than as permitted or required under this Contract*
- *any omission by the Principal to do something which it is obligated to do under this Contract, other than as permitted or required under this Contract*
- *any breach by the Principal of this Contract*

but does not include any act, omission or breach to the extent caused or contributed to by:

- *a Force Majeure Event*
- *the Contractor's breach of this Contract*
- *the negligence or unlawful act or omission of the Contractor or any of its Personnel.*

59 *Rapid Building Group Ltd v Ealing Family Housing Association Ltd* (1984) 29 BLR 5, cited in Eggleston, B., 2009. *Liquidated Damages and Extensions of Time In Construction Contracts*. Wiley Blackwell.

60 Ibid.

61 Ibid.

62 [1984] VR 391

63 Ibid, cited in Pickervance, K., 2006. Calculation of a Reasonable Time to Complete When Time is at Large, *International Construction Law Review*, pp. 167, 177.

64 [2004] SASC 151.

65 Ibid, [12] (Besanko J).

66 *Zhoushan Jinhaiwan Shipyard Co Ltd v Golden Exquisite Inc* [2015] 1 Lloyd's Rep. 283; *Jiangsu Guoxin Corporation Ltd (formerly known as Sainty Marine Corporation Ltd) v Precious Shipping Public Co. Ltd* [2020] EWHC 1030 (Comm).

Infrastructure contracts often also contain clauses which seek to exclude the Prevention Principle outright, for example:

> *'Any principle of law or equity (including the Prevention Principle and those which might otherwise entitle the Contractor to relief), which might otherwise cause the date for commercial operation to be set at large and liquidated damages unenforceable, will not apply.'*
>
> *'For the avoidance of doubt, a delay caused by any act or omission of the Principal or any failure by the Principal or the Principal's representative to comply with this clause will not cause the date for commercial operation to be set at large.'*

The England and Wales Court of Appeal has clarified that the Prevention Principle is an implied term, not 'an overriding rule of public or legal policy'.[67] As such, parties may use express terms to contract out of the Prevention Principle. Coulson LJ stated that:

> *Clause 2.25.1.3(b) was an agreed term. There is no suggestion […] that the parties cannot contract out of some or all of the effects of the prevention principle: indeed, the contrary is plain. Salmon LJ's judgment in Peak v McKinney […] expressly envisaged that, although it had not happened in that case, the parties could have drafted an extension of time provision which would operate in the employer's favour, notwithstanding that the employer was to blame for the delay.*[68]

This view has not yet received judicial confirmation in Australia. However, general principles of law in related areas provide guidance in this area.

The doctrine of freedom of contract means individuals are free to make agreements as they wish, although this can be outweighed by other public policy considerations.[69] Providing an agreement does not offend public policy, it will be enforced on its terms. This was confirmed by the High Court in relation to penalties:[70] exceptions from the doctrine of freedom of contract normally require an element of unconscionability or oppression. By analogy therefore, the Prevention Principle may be excluded in contracts where the parties have expressly agreed upon their risk allocation in terms of time and money.

But the competing argument is that a provision in a contract allowing a Principal to recover damages as a result of its own delay will be viewed by a court as unconscionable. Does this mean that a provision which attempts to exclude the operation of the Prevention Principle may sound in a claim for restitution through the principle of unjust enrichment? It would appear unlikely as the Prevention Principle is not a fundamental equitable principle, and a claim for unjust enrichment in respect of a clause mutually agreed to by the parties would be a highly unusual extension of restitutionary principle.

On balance, the better view is that the Prevention Principle can be contracted out of, provided there is no oppression or disadvantage – and if there is, the doctrine of unconscionability may apply to impose an equitable remedy.

Example regime

An example regime to assist a Principal to avoid the Prevention Principle is set out below.

Drafting example

'Subject to the provisions of this GC [ ], the Contractor is entitled to an extension of time to the Date for Commercial Operation as assessed by the Principal, where a delay to the progress of the Works is caused by any of the following events, whether occurring before, on or after the Date for Commercial Operation:

- *any act, omission, breach or default by the Principal, the Principal's Representative and their agents, employees and contractors (excluding the Contractor and its Subcontractors)*
- *a Variation, except where that Variation is caused by an act, omission or default of the Contractor or its Subcontractors, agents or employees*
- *a Suspension of the Works pursuant to GC [ ], except where that suspension is caused by an act, omission or default of the Contractor or its Subcontractors, agents or employees*
- *[etc].*

Despite any other provisions of this GC [ ], the Principal may at any time and for any reason and whether or not the Contractor has complied with the requirements of GC [ ], extend the Date for Completion. The right to extend the Date for Completion is for the benefit of the Principal only.'



67 *North Midland Building Ltd v Cyden Homes Ltd* [2018] EWCA Civ 1744, [30].

68 Ibid, [36].

69 See *Australian Securities and Investments Commission v Fortescue Metals Group Ltd* [2011] FCAFC 19 at [222]).

70 *Ringrow Pty Ltd v BP Australia Pty Ltd* (2005) 222 ALR 306, 314 (citing *AMEV-UDC Finance Ltd v Austin* (1986) 162 CLR 170 at 190).

5
Proportionate liability

5.1 Introduction

This section provides an overview of the proportionate liability regime which has been enacted in all Australian States and Territories in varying forms, and which represents a significant departure from the common law principles of liability sharing still used in parts of the United Kingdom.

This section also discusses how the regime applies and operates throughout Australia and the change that the regime has made to the common law doctrine of joint, several and joint and several liability for claims for property damage or economic loss arising from carelessness or a failure to take reasonable care. The proportionate liability regime is unfortunately quite complicated with much of the devil in the detail, a difficulty that is enhanced by the many subtle differences across the different jurisdictions. It is beyond the scope of this paper to cover all of the intricacies of the proportionate liability regime, but this section will highlight key aspects of the regime and discuss the slight variances in its application across different Australian jurisdictions.

This section also discusses the history to the introduction of the regime, as well as proposals to introduce a model and uniform law of proportionate liability in Australia.

Knowledge and understanding of the proportionate liability regime are important for commercial and infrastructure lawyers because the contractual risk allocation in infrastructure contracts can be materially altered by operation of the relevant proportionate liability legislation.

5.2 Why was the proportionate liability regime introduced into Australia?

In 1994, concerns about the way in which the common law doctrine of joint and several liability influenced litigation decisions and a perceived crisis regarding the cost of liability insurance prompted an inquiry instituted by the Commonwealth and NSW Attorneys General and conducted by Professor J L R Davis. Specifically, concerns were being voiced by professional and industry bodies that organisations with deep pockets (for example, auditors) or insurers were being targeted in negligence actions not because of their liability (which was often small), but because they were more able to pay large damages awards. A consequence was a significant increase in insurance premiums for liability insurance (especially professional liability). While recommendations for reform were made as a result of that inquiry, they lay dormant until the collapse of the HIH Insurance Group in 2001, which provided the catalyst for change.

5.3 What is the proportionate liability legislation?

In 2003, the Finance Ministers of all Australian jurisdictions agreed to produce uniform national legislation. This was not achieved, however, and proportionate liability legislation was introduced under 11 Acts with a range of differences.

The relevant Acts are set out below.

Jurisdiction	Legislation
Cth	*Competition and Consumer Act 2010 (Cth) – Part VIA (CCA)* *Australian Securities and Investments Commission Act 2001 (Cth) – Part 2, Division 2, Subdivision GA (ASIC Act)* *Corporations Act 2001 (Cth) – Part 7.10, Division 2A (Corporations Act)*
NSW	*Civil Liability Act 2002 (NSW) – Part 4 (NSW Act)*
VIC	*Wrongs Act 1958 (Vic) – Part IVAA (Vic Act)*
WA	*Civil Liability Act 2002 (WA) – Part 1F (WA Act)*
QLD	*Civil Liability Act 2003 (Qld) – Part 2 (Qld Act)*
SA	*Law Reform (Contributory Negligence and Apportionment of Liability) Act 2001 (SA) – Part 3 (SA Act)*
TAS	*Civil Liability Act 2002 (Tas) – Part 9A (Tas Act)*
NT	*Proportionate Liability Act 2005 (NT) (NT Act)*
ACT	*Civil Law (Wrongs) Act 2002 (ACT) – Chapter 7A (ACT Act)*

5.4 What is the effect of the proportionate liability regime and how does it differ from the common law regime?

What are the common law principles on shared liability?

The common law principles on shared liability are as follows:

- **Several liability**: Where two or more parties undertake separate obligations and each is liable only for its own obligations. If one party fails to meet its obligations, the other party is not liable for that failure.
- **Joint liability**: Where two or more parties undertake the same obligation and each is liable in full for the performance of that obligation. In the event of non-performance, the parties would have to be sued jointly, and if one party pays the liability in full, it can require the other parties to pay their share.
- **Joint and several liability**: Where two or more parties undertake the same obligation, action can be taken against and total loss recovered from one wrongdoer, regardless of the extent of its fault and leaving it up to that defendant to seek contribution from the other wrongdoers.

How does proportionate liability differ from the common law?

Where it applies, the proportionate liability regime replaces the common law rules of joint, several and joint and several liability with a system which requires liability for the loss to be apportioned between all the concurrent wrongdoers according to their respective responsibility for the loss. Each concurrent wrongdoer's liability will be limited to the amount of loss attributable to it.

The proportionate liability regime prevents the plaintiff from selecting the defendant(s) with the deepest pockets or those which are insured to recover from, and it 'protects defendants from having to bear more than a just share of liability'.[71] It eliminates the chosen defendant(s)' burden of chasing the other wrongdoers for contribution and transfers the risk of an insolvent wrongdoer from the defendant to the plaintiff.

The way in which the proportionate liability regime interferes with the allocation of contractual risk is illustrated in the following common contractual scenarios:

Scenario	Example	Pre-proportionate liability regime	Post-proportionate liability regime
Co-Contractors	A Principal separately contracts with both an architect and a builder to construct a project. Both have a duty of care to the Principal with respect to the quality of the design, and both are in breach when the design is found to be defective.	Principal can recover 100% of its loss from either party.	Principal only entitled to recover from each party that portion of the loss for which the particular party is responsible.
Head Contractor and sub-contractor	A Principal contracts with a Head Contractor to construct certain works. The Head Contractor subcontracts aspects of the construction. Both Head Contractor and sub-contractor breach their obligation to carry out the works with reasonable skill and care and the Principal suffers loss.	Principal can recover 100% of the loss from the Head Contractor. (Note: the Head Contractor would likely have a contractual right to seek a contribution from the sub-contractor).	Principal only entitled to recover from each party that portion of the loss for which that party is responsible (for example, unable to solely rely on the financial capacity of the Head Contractor).
Co-sellers	A buyer contracts with multiple sellers to purchase shares in a company. The sellers breach a warranty given by them jointly under the sale contract in breach of the State/Federal misleading or deceptive conduct provisions.	Buyer can recover 100% of the loss from one of the sellers.	Buyer only entitled to recover from each seller that portion of the loss for which that seller is responsible.

[71] Clarke QC, G. S., 2019. Proportionate Liability in Commercial Cases: Principles and Practice, *ALJ*, pp. 93, 188, 189.

Where the proportionate liability regime does not apply, the common law principle applies, and a wrongdoer will be jointly and/or severally liable (as the case may be) to the plaintiff for the whole of the plaintiff's loss and must rely on statutory, contractual or equitable rights of contribution or indemnity.

In England and Wales, as in Australia, rising insurance costs prompted debate about the introduction of a proportionate liability regime.[72] However, England and Wales have retained the principle of joint and several liability in the context of breach of contract and construction disputes, with judicial commentary on proportionate liability mainly arising in the context of torts and mesothelioma cases.[73] For example, in *Barker v Corus,*[74] a plaintiff brought an action in tort law after being exposed to asbestos in the course of employment with several employers. Some employers were insolvent. The House of Lords held that the parties were liable in the proportions to which they contributed to the harm.

5.5 When and how does the proportionate liability regime apply?

For the proportionate liability regime to apply, the plaintiff must have brought an 'apportionable claim' against at least one defendant in circumstances where there are other concurrent wrongdoers which may also be liable.

'Apportionable claim'

While an 'apportionable claim' generally requires carelessness, the requirements are expressed differently across the different proportionate liability jurisdictions, which means that the range of claims falling within the proportionate liability regime may vary, particularly in a contractual context.[75]

Carelessness – New South Wales, Victoria, Western Australia, Tasmania, Australian Capital Territory and Northern Territory

Subject to some minor variation, the legislation in these jurisdictions provides that proportionate liability applies to claims for economic loss or damage to property in an action for damages (whether in contract, tort or otherwise), arising from a **failure to take reasonable care**, excluding any claim arising out of personal injury.[76]

There is a live issue around what constitutes an action for damages arising from 'a failure to take reasonable care' and, by extension, how the proportionate liability regime applies to claims based on breach of a strict contractual obligation or warranty.

On one interpretation, the legislation only applies to contractual claims where there is a breach of an express or implied contractual term requiring the defendant to exercise reasonable care, for example, a contractual duty of care. On this interpretation, apportionment would not be available in a claim for breach of a strict contractual duty or warranty, even if the breach were caused by a failure to take reasonable care. No court has yet applied such a narrow interpretation, although such an interpretation is not without support.[77]

The alternative interpretation (supported by a string of cases in **New South Wales** and **Victoria**)[78] is that proportionate liability applies to any breach of contract provided the conduct giving rise to the breach originates in a failure to take reasonable care. The key question is whether, as a matter of fact, the cause of action originates from some carelessness by the defendant and does not depend on establishing a breach of any duty of care.

In the New South Wales Court of appeal decision in *Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)*,[79] Macfarlan JA stated that for an action to have arisen from a failure to take reasonable care, it was necessary for that failure to be an element of the cause of action relied on and that 'if claims could be apportioned where negligence is not an element of the successful cause of action, but merely arises from the facts, a plaintiff could lose his or her contractual right to full damages from a party whose breach of a contractual provision of strict liability happened to stem from a failure to take reasonable care'.[80] Barrett J disagreed[81] (and referred to his reasoning in *Reinhold v NSW Lotteries Corporation (No 2)*,[82] and Meagher JA preferred not to express a view on the issue (although he noted that the claim which may or may not arise out of a failure to take reasonable care is one which has been determined and established as a source of liability).[83]

72 Professor Doug Jones, 'Proportionate Liability Revisited' - lecture delivered on 17 November 2020, at page 13.

73 Ibid.

74 [2006] 2 AC 572.

75 Note: the SA Act refers to 'apportionable liability'.

76 See NSW Act s 34(1) and s 34(3); ACT Act s 107B(2) and s 107B(3); NT Act s 4(2) and s 4(3); Tas Act s 43A(1), s 43A(8) and s 3B; WA Act, s 5AI(a), s 5AJ(2) and s 3A; and Vic Act s 24AF(1) and s 24AG(1).

77 See for example the comments of Biscoe AJ (in an ex tempore judgment on an application for leave to amend a pleading during a trial) in *Pfizer Australia Pty Ltd v Probiotec Pharma Pty Ltd* [2010] NSWSC 532 at [8]. See also McDonald, B., 2011. Indemnities and the Civil Liability Legislation, *Journal of Contract Law*, 27, *56* in which she argues that such an interpretation 'leads to the absurd result that it would now be advantageous for a defendant to plead negligence in cases where he or she is sued for breach or a warranty or strict obligation'.

78 See *Woods v De Gabriele* (2007) 2 BFRA 168: [2007] VSC 177, *Dartberg Pty Ltd v Wealthcare Financial Planning Pty Ltd* (2007) 164 FCR 450: [2007] FCA 1216, and *Reinhold v NSW Lotteries Corporation (No 2)* [2008] NSWSC 187.

79 [2013] NSWCA 58.

80 [2013] NSWCA 58 at [22].

81 [2013] NSWCA 58 at [37]–[42].

82 [2008] NSWSC 187.

83 [2013] NSWCA 58 at [35]–[36].

Following *Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)*,[84] it remains uncertain whether a court will find that a claim is an apportionable claim due to the facts where it is uncertain whether the cause of action requires a failure to take reasonable care (although a court is likely to closely scrutinise pleadings that appear to have been deliberately phrased to exclude the proportionate liability regime).[85]

Carelessness – Queensland and South Australia

The language used in the Queensland and South Australian legislation is different. In Queensland, the regime only applies if there is a claim for economic loss or property damage 'arising from a breach of a duty of care'.[86] Whereas in South Australia, the regime only applies to a liability in damages that arises under the law of torts or under statute or 'for breach of a contractual duty of care'.[87]

There is presently no case law on these provisions, but they appear to reduce proportionate liability (in a contractual context) to a much narrower scope than in other jurisdictions.[88]

Misleading or deceptive conduct

An 'apportionable claim' also includes claims for economic loss or damage in an action for misleading or deceptive conduct under designated State or Federal legislation (not limited to a failure to take reasonable care).[89]

In *Selig v Wealthsure Pty Ltd*,[90] the High Court confirmed the scope of the proportionate liability regime in Division 2A of Part 7.10 of the *Corporations Act*, thereby resolving the conflicting judgments delivered by differently constituted Full Federal Courts in *Wealthsure Pty Ltd v Selig*[91] and *ABN Amro Bank NV v Bathurst Regional Council*[92] in 2014.

The Seligs brought several claims against Wealthsure Pty Limited for breaches of the prohibition against misleading or deceptive conduct in relation to financial products or services in section 1041H of the *Corporations Act* and section 12DA of the *ASIC Act* (which were apportionable claims), as well as other provisions of the *Corporations Act* and other statutes, and for breach of contract and negligence (which were not apportionable claims).

The High Court held that a defendant whose conduct renders it:

- liable for damages for misleading or deceptive conduct which contravenes section 1041H of the *Corporations Act*
- liable for damages on other bases (including other contraventions of the *Corporations Act*)

may be liable for the whole of the plaintiff's loss caused by that conduct, notwithstanding the application of the proportionate liability regime to the s1041H claim. In so finding, the High Court held that an apportionable claim under section 1041L of the *Corporations Act* is only a claim for damages caused by misleading or deceptive conduct which contravenes section 1041H, and does not extend to other claims for damages on other bases, even where the damages claims are brought in parallel with the misleading or deceptive conduct claim and are based on the same loss or conduct.[93]

The High Court's reasoning also applies to equivalent proportionate liability provisions in the *ASIC Act* and to the contributory negligence defence in s1041I(1B) of the *Corporations Act*.

Following this, in *Williams v Pisano*,[94] the New South Wales Court of Appeal (albeit in obiter) applied the High Court's reasoning in *Selig v Wealthsure Pty Ltd* to the proportionate liability regime in Part VIA of the *Competition and Consumer Act 2010* (Cth) (CCA). The Court stated that where a party is liable for contravening both section 18 and section 30 of the Australian Consumer Law (Schedule 2 of the CCA), the party's liability under section 30 is not apportionable because an apportionable claim under section 87CB of the CCA is only a claim for damages caused by misleading or deceptive conduct which contravenes section 18 of the Australian Consumer Law.[95]

The *Selig* decision is not good news for defendants who are only able to enjoy the protection of:

- the proportionate liability and contributory negligence regimes in Division 2A, Part 7.10 of the *Corporations Act* to the extent that the plaintiff alleges a breach of section 1041H of the *Corporations Act*
- the proportionate liability regime in Subdivision GA of Division 2, Part 2 of the *ASIC Act* to the extent that the plaintiff alleges a breach of section 12DA of the *ASIC Act*.

Similarly, while the comments of the New South Wales Court of Appeal in *Williams v Pisano* were obiter, they signal a comparable approach by the Court that defendants are only able to enjoy the protection of the proportionate liability regime in Part VIA of the CCA to the extent that the plaintiff alleges a breach of section 18 of the Australian Consumer Law.

While courts have not yet referred to other legislation, the logical application of these decisions is that courts will take a literal reading of any legislative definition of an 'apportionable claim'.

84 The special leave application to the High Court was dismissed: [2013] HCATrans 248.

85 Courts will be slow to resolve such issues summarily because of the complexity and uncertainty of the debate involved: see for example *ASF Resources Ltd v Clarke* [2014] NSWSC 252 per Kunc J.

86 Qld Act s 28(1)(a).

87 SA Act s 4(1). section 2 of the SA Act refers to negligent or innocent liability for harm.

88 See Joshua Thompson, Leigh Warnick and Ken Martin, *Commercial Contract Clauses: Principles and Interpretation*, Thompson Reuters – Legal Online at para [26130] for further discussion of the position in Queensland and South Australia.

89 NSW Act s 34(1)(b); ACT s 107B(2)(b); Tas Act s 43A(1)(b); WA Act s 5AI(b); NT Act s 4(2)(b); SA Act s 3(2)and s 4(1)(c) (by implication); Vic Act s 24AF(1)(b); ASIC Act s 12GP(1); Corporations Act s 1041L(1) and CCA s 87CB(1). However, note that the second limb of s 24AF of the Vic Act refers to 'a claim for damages for a contravention of section 18 of the Australian Consumer law (Victoria)' without stating that it must also be a claim for economic loss or property damage.

90 [2015] HCA 18.

91 [2014] FCAFC 64.

92 [2014] FCAFC 65.

93 See [22] to [38] per French CJ, Kiefel, Bell and Keane JJ; [51]-[57] per Gageler J.

94 [2015] NSWCA 177.

95 See [55] to [64].

The defendant must be a concurrent wrongdoer

A concurrent wrongdoer is generally defined broadly to include one of two or more persons whose acts or omissions caused, independently of each other or together, the loss or damage that is the subject of the claim.[96] However, in **Queensland** and **South Australia**, the relevant persons must have acted independently of each other and not jointly.[97]

A defendant seeking to limit its liability under the proportionate liability regime bears the onus of pleading and proving that it is only partially to blame for the plaintiff's loss, and that there are other concurrent wrongdoers which also bear some responsibility.[98]

There have been numerous cases dealing with the issue of who is a concurrent wrongdoer and whether a person has caused the 'loss or damage that is the subject of the claim'. These cases culminated in the 2013 decision in *Hunt & Hunt Lawyers v Mitchell Morgan Nominees Pty Ltd*[99] in which the High Court adopted a more liberal interpretation as to the meaning of 'loss or damage' for the purposes of the NSW Act and confirmed that independent and unrelated acts which both cause the same damage can be apportioned. In that case, on the basis of fraudulently obtained certificates of title and forged documentation presented by Mr Caradonna and Mr Vella (the fraudsters), Mitchell Morgan Nominees Pty Ltd (**MM**) advanced money which was secured by mortgage. The mortgage was negligently drafted by Hunt & Hunt lawyers to secure money owed by Mr Vella (and not Mr Caradonna) and therefore secured nothing.

The majority of the High Court reinstated the trial judge's decision (overturning the Court of Appeal decision) and apportioned 72.5% liability to Mr Caradonna, 15 % to Mr Vella and 12.5% to Hunt & Hunt.[100] The basis for the High Court's decision was that it did not matter that MM had different causes of action against Hunt & Hunt (for negligent drafting) and the fraudsters. The harm that MM suffered was the inability to recover the money and, so long as the acts of each wrongdoer were a material cause of that harm, they were concurrent wrongdoers (despite the legal bases of those claims).

The High Court also distanced itself from the decision in *St George Bank Ltd v Quinerts Pty Ltd*,[101] which involved a negligent valuation and a subsequent mortgage default which left the Bank with a loss of more than AUD$100,000. In that case, the Victorian Supreme Court held that for the purposes of identifying concurrent wrongdoers, the damage or loss caused must be the 'same damage' (and that the only actionable acts or omissions by the borrower and the Guarantor was the failure to repay the loan and that such failures did not cause the Bank to make the loan). However, the High Court was not prepared to delve into whether or not *Quinerts* was wrongly decided and so it remains law, particularly in relation to negligent valuations.[102]

The decision in *Hunt & Hunt* is good news for defendants and insurers who will find it easier to establish that there were other concurrent wrongdoers responsible for the loss or damage the subject of the claim, and thus limit their liability under the proportionate liability regime. At this stage, whether or not parties are 'concurrent wrongdoers' continues to depend on a detailed analysis of the claims against each of them and a careful characterisation of the loss caused by each of them. However, a plaintiff wishing to target a particular party will need to ensure that their claim focuses on the particular loss or damage caused, to help show that a concurrent wrongdoer's conduct did not cause the same loss or damage as the targeted defendant.

Proportionate liability must not be excluded from the claim

There are a number of categories of claims which are excluded from the proportionate liability regime, which are set out below (although not all of these exclusions apply in every jurisdiction):

- intentional or fraudulent conduct[103]
- where proportionate liability is excluded by other legislation[104]
- vicarious liability and the liability of a partner[105]
- agency[106]
- consumer claims[107]
- exemplary or punitive damages[108]
- claims arising from personal injury[109]
- criminal proceedings[110]
- the right to contract out[111] (see section 5.6 'Contracting out of the proportionate liability regime' below).

96 NSW Act s34(2), ACT Act ss 107A and 107D; NT Act ss 3 and 6(1); Tas Act s 43A(2); Vic Act s24AH; WA Act s 5AI; ASIC Act s 12GP(3); Corporations Act s 1041L(3) and CCA s 87CB(3).

97 Qld Act s 30 and SA Act s 3(2)(b). Note also that the SA Act uses the term 'wrongdoer' instead of 'concurrent wrongdoer' (s3 of the SA Act).

98 *Dartberg Pty Limited v Wealthcare Financial Planning Pty Ltd* (2007) 164 FCR 450 at [31] and *Polon v Dorian* [2014] NSWSC 571 at [812].

99 [2013] HCA 10; (2013) 246 CLR 613.

100 French CJ, Hayne and Keifel JJ.

101 (2009) 25 VR 666. See also *Shrimp v Landmark Operations Ltd* (2007) 163 FCR 510; [2007] FCA 1468.

102 See also *Hadgelias Holdings Pty ltd v Seirlis* [2014] QCA 117 where Holmes JA (with whom Gotterson and Morrison JJA agreed) explained the definition of concurrent wrongdoer in s87CB(3) of the *Trade Practices Act 1974* (Cth) (now s87CB(3) of the CCA) as 'concerned with distinct acts (or omissions) or sets of acts (or omissions) by different actors, combining or working independently to cause loss or damage, and consequently inapplicable where there is but a single act or set of acts causing loss, attributable to more than one person'. This approach has been questioned. For example, Joshua Thompson, Leigh Warnick and Ken Martin, *Commercial Contract Clauses: Principles and Interpretation*, Thompson Reuters – Legal Online at para [25770].

103 NSW Act s 34A(1)(a) & (b); ACT Act s 107E(1); NT Act s 7(1); Qld Act ss 32D & 32E, SA Act s 3(2)(c); Tas Act s 43A(5); Vic Act s 24AM; WA Act s 5AJA(1)(a) & (b); ASIC Act s 12GQ(1)(a) & (b); Corporations Act s 1041M(1)(a) & (b); CCA s 87CC(1)(a) & (b).

104 NSW Act s 39(c); ACT Act ss 107B(4) and 107K(d); NT(c) Act s 14(c); Qld Act s 28(4) & (5); Tas Act s 43G(1)(c); Vic Act ss 24AF(3) (fraudulent conduct only), 24AG(2) and 24AP(e); WA Act ss 5AJA(1)(c) & 5AO(c); ASIC Act s 12GW (c); Corporations Act s 1041S(c); and CCA s 87CI(c).

105 NSW Act s 39(a) & (b); ACT Act s 107K; NT Act s 14(a) & (b); Qld Act s 32I(a) & (c); SA Act s 3(1) 'derivative liability'; Tas Act s 43G(1)(a) & (b); Vic Act s 24AP(a) & (c); WA Act s 5AO(a) & (b); ASIC Act s 12GW (a) & (b); Corporations Act s 1041S(a) & (b); CCA s 87CI(a) & (b).

106 ACT Act s 107K(b); Qld Act s 32I(b); Vic Act s 24AP(b).

107 ACT Act s 107B(3)(b); Qld Act s 28(3)(b).

108 Qld Act s 32I(d); SA Act ss 3(1) (see definition of 'notional damages'), 3(3) & 8(6); and Vic Act s 24AP(d).

109 NSW Act s 34(1)(a); ACT Act s 107B(3)(a); NT Act ss 3 definition of 'economic loss' and 4(3)(a); Qld Act s 28(3)(a); SA Act ss 3(2)(a)(i) & 8(6); Tas Act s 43A(1); Vic Act s 24AG(1); and WA Act s 5AI(1)(a).

110 SA Act s 4(2).

111 NSW Act s 3A(2); Tas Act s 3A(3) and WA Act s 4A.

Apportionment

If the proportionate liability regime applies, then liability for a plaintiff's loss is apportioned by the courts between all concurrent wrongdoers according to their respective responsibility for the loss.

Each concurrent wrongdoer's liability is then limited to the amount of loss apportioned to it. The proportionate liability legislation operates to restrict the courts, when ordering damages, to such amounts as the court considers 'just', having regard to each concurrent wrongdoer's responsibility, and no more.[112]

What factors the court must take into account in determining what is 'just' will depend upon the facts of the case, but it seems the courts are guided by the apportionment principles used for contributory negligence,[133] noting they must exclude the extent to which the plaintiff's contributory negligence caused the loss or damage.[114] The relative financial capacity of concurrent wrongdoers is not a factor to be considered.[115] A more recent consideration of the apportionment factors was by Judge Woodward in the Lacrosse Tower case.[116]

Identifying and joining all possible concurrent wrongdoers

Courts may (and in **Western Australia, Tasmania and South Australia**, must) look to the proportionate responsibility of absent defendants.[117] In **Victoria**, the legislation is silent on this issue because under subsection 24AI(3), a court is only permitted to take into account the comparative responsibility of a non-party who has died or a corporation that has been wound up.[118]

A court has the power to grant leave for a concurrent wrongdoer to be joined as a defendant.[119]

Except in **Victoria**, plaintiffs must identify and join everyone legally responsible to ensure the recovery of 100% of their loss. To facilitate this, a concurrent wrongdoer must inform the plaintiff if it has reasonable grounds to believe that a particular person may also be a concurrent wrongdoer in relation to the relevant claim. This is not a duty to inform as such, but if a concurrent wrongdoer fails to do this, it may be liable for any costs incurred by the plaintiff because it was not aware of such additional concurrent wrongdoer.[120] In Victoria, the defendants must ensure that all concurrent wrongdoers have been joined as parties to the proceedings.

Contribution between concurrent wrongdoers

The legislation in all jurisdictions (apart from **South Australia**) provides that a defendant against whom judgment is given as a concurrent wrongdoer in relation to an apportionable claim cannot be required to:

- contribute to any damages or contribution recovered from another wrongdoer in respect of that apportionable claim (in **Victoria** and the **Northern Territory**, the damages must have been recoverable in the same proceedings in which judgment was given against the defendant, whereas in other jurisdictions, it does not matter whether or not the damages were recovered in the same proceedings)
- indemnify any such wrongdoer.[121]

Importantly, this protection only applies to concurrent wrongdoers against whom judgment is given in relation to an apportionable claim. As such, defendants who settle with a plaintiff ought to consider the relative benefits of having judgment entered against them.

Subsequent claims

A plaintiff who has previously recovered judgment against a concurrent wrongdoer for an apportionable part of any claim for damage or loss is not prevented from subsequently bringing another action against another wrongdoer, provided the plaintiff cannot recover in total more than the damage or loss sustained by the plaintiff.[122]

However, a plaintiff risks recovering less than their total loss if separate actions are run because courts are not bound to find the same proportionate responsibility for the later defendant to that which was apportioned by the court in an earlier proceeding.

The scope of s12GU of the ASIC Act was considered in City of Swan v McGraw-Hill Companies Inc.[123] In that decision Rares J found that the proportionate liability regime does not envisage that quantification of the claimant's damages will necessarily be finalised in the first proceedings and, instead, subsequent proceedings can arrive at different apportionments for other concurrent wrongdoers not joined in the original proceedings.

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112 NSW Act s 35(1);ACT finalised s 107F(1)(a); NT Act s 13(1)(a); Qld Act s 31(1)(a) (although note that the reference is to 'just and equitable' as opposed to 'just'); SA Act s 8(2)(a) (although note that there reference is to 'fair and equitable' as opposed to 'just'); Tas Act s 43B(1)(a); Vic Act s 24AI(1)(a); WA Act s 5AK(1)(a); ASIC Act s 12GR(1)(a); Corporations Act s 1041N(1)(a); and CCA s 87CD(1)(a).

113 Professor Doug Jones, 'Proportionate Liability Revisited' - lecture delivered on 17 November 2020, at page 10.

114 NSW Act s 35(3)(a); ACT finalised s 107F(2)(a); Vic Act s 24AN; NT Act s 13(2); Qld Act s 32G; Tas Act s 43B(3)(a); WA Act s 5AK(3)(a); ASIC Act s 12GR(3)(a); Corporations Act s 1041N(3)(a); CCA s 87CD(3)(a).

115 *Reinhold v. New South Wales Lotteries Corporation (No. 2)* [2008] NSWSC 187 per Barrett J.

116 *Owners Corporation No. 1 of PS613436T v. LU Simon Builders Pty Ltd (Building and Property)* [2019] VCAT 286.

117 NSW Act s 35(3)(b); ACT finalised s 107F(2)(b); NT Act s 13(2)(b); Qld Act s 31(3); SA Act s 8(2)(b); Tas Act s 43B(3)(b); WA Act s 5AK(3)(b); ASIC Act s 12GR(3)(b); Corporations Act s 1041N(3)(b); CCA s 87CD(3)(b).

118 Vic Act s24AI(3).

119 NSW Act s 38; ACT finalised s 107J; NT Act s 11; Qld Act s 32H; SA Act s 11; Tas Act s 43F; Vic Act s 24AL; WA Act s 5AN; ASIC Act s 12GV; Corporations Act s 1041R; CCA s 87CH. Leave will be granted even if only declaratory relief is sought against a concurrent wrongdoer. For example, *Fudlovski v JGC Accounting & Financial Services Pty Ltd (No 3) [2013] WASC 476 and also Lion-Dairy & Drinks Pty Ltd v Sinclair Knight Merz Pty Ltd* [2014] FCA 386.

120 NSW Act s35A (despite the section being titled 'Duty…to inform..'); ACT Dudovskiy s 107G; NT Act s 12; Qld Act s 32; SA Act s 10; Tas Act 43D; WA Act s 5AKA; ASIC Act s 12GS; Corporations Act s 1041O; CCA s 87CE.

121 See NSW Act s36. ACT Dudovskiy s 107H; NT Act s 15; Qld Act s 32A; SA Act s 9; Tas Act s 43C; Vic Act s 24AJ; WA Act s 5AL; ASIC Act s 12GT; Corporations Act s 1041P; CCA s 87CF are also in a similar form. Note that SA Act s 9(a) also provides that wrongdoers who are part of the same group are to be treated as a single wrongdoer.

122 Under the NSW Act s 37; ACT the Act s 107I; the NT Act s 16; the Qld Act s 32B; the Tas Act s 43E; Vic Act s 24AK; the WA Act s 5AM; the ASIC Act s 12GU; the Corporations Act s 1041Q and the CCA s 87CG, the plaintiff's rights are expressly preserved. The position under s 11 of the SA Act is different and may be broader in scope. It does not expressly preserve the plaintiff's rights but starts from the premise that such actions may be brought.

123 [2014] FCA 442 at para 63.

5.6 Contracting out of the proportionate liability regime

Is it possible to contract out?

A key issue for parties to an infrastructure contract in Australia to consider is whether they should agree to 'contract out' of the applicable proportionate liability regime, that is, to expressly agree in the contract that the proportionate liability regime will not apply. On this issue, as between the different jurisdictions in Australia, there are various approaches:

- **New South Wales, Western Australia and Tasmania:** The proportionate liability legislation in these jurisdictions permits contracting out – expressly in Western Australia and by implication in New South Wales and Tasmania[124]
- **South Australia, Victoria, Australian Capital Territory and Northern Territory:** The proportionate liability legislation in these jurisdictions is silent about contracting out. There is a significant risk that contracting out is not permitted because it is arguably inconsistent with the public policy underpinning proportionate liability[125]
- **Commonwealth misleading or deceptive conduct legislation:** The proportionate liability legislation in this jurisdiction is the same as South Australia, Victoria, Australian Capital Territory and Northern Territory. It is generally accepted that it is not possible for parties to limit or exclude their liability for breach of the statutory misleading or deceptive conduct prohibitions
- **Queensland:** The proportionate liability legislation in this jurisdiction prohibits contracting out.[126]

Should parties contract out?

Whether it is more beneficial to allow the proportionate liability regime to operate, or to exclude or modify its operation by contract (in those jurisdictions where it is currently permitted to do so), will depend on the party you are acting for. As a general rule, the proportionate liability regime benefits supplier defendants rather than customer plaintiffs – the blame is shared, and the losses distributed. However, a customer plaintiff is generally better off excluding the proportionate liability regime because, in the event that it needs to sue a supplier/Contractor, it is preferable to deal only with a single wrongdoer, namely the party it has contracted with, as opposed to also having to sue a number of other entities who may be unknown and of which there may be many.

How do parties contract out?

Where contracting out is permitted, there is a number of ways the parties can achieve this. For instance:

- by including an express clause which states that the relevant proportionate liability legislation does not apply
- by including provisions that have the effect of proportioning liability between the parties in a way that is inconsistent with the proportionate liability regime.[127] For example, a statement that the parties are jointly and severally liable, a statement that a Head Contractor is liable for the acts and omissions of its Sub-contractors,[128] or a statement that one party agrees to indemnify the other in relation to particular liabilities.

There has historically been some debate around whether a contractual indemnity alone is sufficient to constitute contracting out. However, the New South Wales Court of Appeal in *Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)*[129] found that an indemnity by CTC Group Pty Ltd in favour of Perpetual Trustee Company Ltd for loss suffered by Perpetual as a result of a breach of warranty by CTC Group was sufficient to constitute contracting out under section 3A(2) of the NSW Act, and that to find otherwise would have deprived Perpetual of its contractual right to full indemnity for its loss.[130]

Indemnities and potential insurance issues

If an insured party to a contract contractually assumes joint and several liability of an obligation to indemnify in respect of a claim which would otherwise be apportionable, it may be assuming a liability that would otherwise not have arisen at law. Most liability insurances will exclude protection for contractually assumed liability that would not ordinarily arise at law. Therefore, before contracting out in this way, parties should consider whether their insurers need to be aware of and accept this proposed risk allocation.

Exclusion clauses

In **Western Australia, New South Wales** and **Tasmania**, where contracting out is permitted, an exclusion clause, whereby a defendant excludes all liability for breach of contract and negligence, would not seem to be affected by the proportionate liability regime.

Similarly, in **South Australia,** courts are expressly directed to take into account any special limitation of liability (which is defined to include a limitation under a contract) to which a defendant may be entitled and, as such, would not seem to affect the operation of an exclusion clause.[131]

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124 WA Act s 4A (which includes an express statement that contracting out is permitted) and NSW Act s 3A(2) and Tas Act s 3A(3) (where the ability to contract out is not as clear cut as in WA but the relevant sections state that parties are not prevented from making express provisions for their rights, obligations and liabilities and the relevant Acts do not affect the operation of such express provisions). Courts have expressed the view that the provisions in the NSW Act and the Tas Act permit contracting out. See for example, *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3 at [19] and *Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)* [2013] NSWCA 58 at [11]-[12]. Legal commentators also agree with this position. For example, Hayford, O., 2010. Proportionate Liability – Its Impact on Contractual Risk Allocation, *Building and Construction Law Journal,* 26, 11 at 24 and McDonald, B., 2005, Proportionate Liability in Australia: The Devil in the Detail, *Australian Business Review*, 26, *29.*

125 For example, Joshua Thompson, Leigh Warnick and Ken Martin, *Commercial Contract Clauses*: *Principles and Interpretation*, Thompson Reuters – Legal Online at para [26790].

126 Qld Act s 7(3) (the Qld Act does not prohibit contracting out entirely, but only in relation to Chapters 2 (which contain proportionate liability provisions) and 3).

127 The Tasmanian Full Court held in *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3 at [19] that parties can contract out just by adopting an allocation of liability wording that is inconsistent with the proportionate liability regime, and without referring specifically to the proportionate liability regime. See also the Western Australia District Court in *Owners of Strata Plan 13259 v Fowler* [2013] WADC 5 (noting its limited precedential value) and the new South Wales Court of Appeal in *Perpetual Trustee Company Ltd v CTC Group Pty Ltd (No 2)* [2013] NSWCA 58.

128 This was the relevant contractual provision considered in *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3.

129 [2013] NSWCA 58.

130 Further, the Tasmanian Full Court in *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3 at [16] observed that the 'plain purpose' of s 3A(c) (the Tas Act equivalent of section 3A of the NSW Act) was 'to ensure the primacy of express provisions of a contract as to the parties' rights, obligations and liabilities under the contract, over any provision in relation to the same matter in the Act'.

131 SA Act s 8(4)(d).

In **Queensland**, where contracting out of proportionate liability is prohibited, the legislation is expressed to 'limit' the liability of a concurrent wrongdoer.[132] As such, it is arguable because the Qld Act deals with the limitation of liability (and not the *imposition* of liability), there is no reason why liability should not be excluded altogether.[133] If such an argument is valid under the Qld Act, it should also be valid in **Victoria**, the **Australian Capital Territory** and the **Northern Territory**, where the legislation is silent on contracting out and are similarly expressed to limit the liability of a concurrent wrongdoer.[134]

Other possible indirect methods of contracting out

Other, indirect, ways in which the parties may be able to effectively contract out of the proportionate liability regime include:

- by choosing a governing law clause that is in a state where contracting out is permitted – namely **Western Australia, New South Wales** and **Tasmania**) – there is a risk in pursuing this strategy if the chosen jurisdiction and the contract are not sufficiently connected[135]
- by agreeing to arbitrate disputes under a contract – it is unclear whether arbitration is subject to the proportionate liability legislation.[136] If it is not, it may be possible to avoid proportionate liability in this way, although, for the sake of clarity, it is prudent to include an express provision in the contract that the proportionate liability regime does not apply to the arbitration
- possibly, by creating separate legal relationships or collateral arrangements with parties which may be found to be proportionately liable, for example, a Principal could enter into a deed with a sub-contractor pursuant to which the sub-contractor promises to the Principal that it will exercise due care in carrying out its obligations to the head Contractor. The Principal would then have a direct cause of action against the sub-contractor in the event that a claim for defective work against the head Contractor is met with a defence that the defects were caused by the sub-contractor. However, in the absence of a direct contractual relationship with the sub-contractor, the Principal may, nonetheless, be able to establish that the sub-contractor owed a duty of care to the Principal in carrying out the works contractually via the head Contractor.

5.7 Indemnities between concurrent wrongdoers

Are indemnities between concurrent wrongdoers permitted?

The availability of indemnities between concurrent wrongdoers depends on the relevant jurisdiction.

As noted in section 5.5 (Contribution between concurrent wrongdoers), the legislation in all jurisdictions (other than South Australia) provides that a defendant against whom judgment is given (as a concurrent wrongdoer in relation to an apportionable claim), cannot be required to indemnify any other wrongdoer for any damages or contribution recovered from that concurrent wrongdoer in respect of that apportionable claim.[137]

In **Tasmania, Western Australia** and the **Northern Territory**, the right to re-allocate liability through contractual indemnities is also expressly preserved.[138]

In other jurisdictions, a strict reading of the language above would operate to prevent a defendant from being required to indemnify a concurrent wrongdoer pursuant to a contractual right of indemnity. The position has not been judicially considered and remains unsettled. Commentators have used various analyses to argue that this is not the intention. For example, McDonald highlights the importance of looking at the proportionate liability legislation in juxtaposition with the legislation it replaces. If this is done, she argues, it can be seen that the restriction is on the power of the courts under the former legislation to order contribution or an indemnity as part of the apportionment process.[139] Furthermore, there is no *'obvious reason of policy or justice which should prevent a defendant from enforcing a voluntarily entered, pre-existing contractual arrangement against another'*.[140] Conversely, Hayford argues that the limitation only applies to requirements arising under common law or statutory rights of indemnity,[141] as opposed to contractual requirements, and Watson argues that the limitation only applies to indemnities which are sought after judgement is given.[142]

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132 Qld Act s31(1)(a).

133 See Joshua Thompson, Leigh Warnick and Ken Martin, *Commercial Contract Clauses: Principles and Interpretation*, Thompson Reuters – Legal Online at para [27020].

134 Ibid.

135 For further discussion on choice of law as an indirect method of contracting out, see Joshua Thompson, Leigh Warnick and Ken Martin, *Commercial Contract Clauses: Principles and Interpretation*, Thompson Reuters – Legal Online at paras [26910] to [26970].

136 In *Curtin University of Technology v Woods Bagot Pty Ltd* [2012] WASC 449, the Western Australia Supreme Court decided that the WA Act did not apply to commercial arbitrations as the word 'court' in the WA Act did not comfortably encompass arbitrators. While this decision was based on the WA Act, it would seem likely that the reasoning would also apply to the other proportionate liability legislation. The court also left open the possibility that the implied term in every arbitration agreement that the arbitrator should decide the dispute according to the existing law of the contract meant that the proportionate liability regime applied. Earlier, in *Aquagenics Pty Ltd v Break O'Day Council* [2010] TASFC 3, the Tasmanian Full Court (in obiter) also favoured the view that the proportionate liability regime under the Tas Act did not apply to arbitrations.

137 In Victoria and the Northern Territory, the damages must have been recoverable in the same proceedings in which judgement was given against the defendant, whereas in the other jurisdictions, it does not matter whether or not the damages were recovered in the same proceedings).

138 Tas Act s 43C; WA Act s 5AL(2); NT Act s 15(2).

139 See McDonald, B., 2011. Indemnities and the Civil Liability Legislation, *Journal of Contract Law*, pp. 27, 56.

140 Ibid.

141 Hayford, O., 2005. Proportionate liability – Its Impact on Contractual Risk Allocation, *Australian Business Review*, 29 at 44.

142 Watson, J., 2004. From Contribution to Apportioned Contribution to Proportionate Liability, *Australian Law Journal*, 78, *126.*

In **New South Wales**, section 3A of the NSW Act specifically acknowledges that contracting parties may make express provisions for their rights, obligations and liabilities to which the proportionate liability regime applies. Arguably this means that contractual indemnities can be enforced against a concurrent wrongdoer.[143]

In **Queensland**, the same provision applies about making express provisions, but includes an express carve out for the proportionate liability regime. This suggests that contractual indemnities that re-apportion loss between concurrent wrongdoers will not be enforced in Queensland.[144]

In **Victoria** and the **Australian Capital Territory**, the proportionate liability regime does not include the additional express acknowledgment that contracting parties may make express provision for their rights, obligations and liabilities. As such, the position is less clear and despite the arguments of commentators outlined above, the question remains that it was open to legislatures to include similar provisions to other jurisdictions, but they chose not to.[145]

In **South Australia**, indemnities are approached differently but the result seems to be that a contractual indemnity can be enforced against a concurrent wrongdoer, even where proportionate liability applies.[146]

Do indemnities between concurrent wrongdoers breach the prohibition on contracting out?

The next question is whether contractual indemnities between concurrent wrongdoers breach the 'no contracting out position' in **Queensland** (and most likely **Victoria, South Australia, Australia Capital Territory** and the **Northern Territory**).

This point is arguable but commentators such as Barbara McDonald, who are in favour of the availability of indemnities, point to the fact that *'the primary liability of either wrongdoer to the plaintiff is not affected' and that 'the common objection to allowing contracting out – That it enables powerful commercial clients to use their market power to insist on solitary liability and to undermine the effectiveness and benefits of the regime…does not apply where it is the potential defendants who have sorted out the allocation of risk between themselves in advance'.*[147]

Indemnities given by non-concurrent wrongdoers

The proportionate liability regime does not operate to restrict indemnities given by a party who did not contribute to the loss (and is not a concurrent wrongdoer). These parties fall outside of the apportionment process under the proportionate liability regime.

5.8 Summary of jurisdictional differences

As noted throughout this paper, there are a number of important legislative inconsistencies between jurisdictions which raise the potential for forum shopping.

For ease of reference, we set out below a summary of the key differences across the different jurisdictions.





143 NSW Act s 3A(2). See further Dominic Villa, *Annotated Civil Liability Act 2002 (NSW)* (Lawbook Co, Second edition 2013), para 4.36.020.

144 Qld Act s 7(3).

145 See Joshua Thompson, Leigh Warnick and Ken Martin, *Commercial Contract Clauses: Principles and Interpretation*, Thompson Reuters – Legal Online at para [26550].

146 SA Act ss 6(1), 6(3), 6(5), 6(9)(a) and 9 and Pt 2 and Pt 3.

147 See McDonald, B., 2011. Indemnities and the Civil Liability Legislation, *Journal of Contract Law*, 27, *56.*

Scenario	NSW	VIC	QLD	WA	SA	TAS	ACT	NT
If acting for a plaintiff, concurrent wrongdoers should be joined as parties to an action	✔	□	✔	✔	✔	✔	✔	✔
If acting for a defendant, concurrent wrongdoers should be joined as parties to an action	□	✔	□	□	□	□	□	□
Concurrent wrongdoers acting jointly (as well as independently) are caught	✔	✔	□	✔	□	✔	✔	✔
Applies to contractual breaches regardless of whether there has been a breach of a duty of care (although there is some debate)	✔	✔	□	✔	□	✔	✔	✔
Intentional wrongdoing excluded (note fraudulent wrongdoing is excluded in all jurisdictions)	✔	□	✔	✔	✔	✔	✔	✔
Proportionate liability excluded as between Principal and agent	□	✔	✔	□	□	□	✔	□
Proportionate liability does not override the award of exemplary or punitive damages	□	✔	✔	□	✔	□	□	□
Exclusion clause can be used to exclude liability for negligence and breach of contract	✔	?	?	✔	✔?	✔	?	✔
Reapportionment through contractual indemnities between wrongdoers permitted	✔	□	□	✔	✔	✔	□	✔
Contracting out permitted	✔	?	□	✔	?	✔	?	?



5.9 Proportionate liability reform

The lack of consistency in the proportionate liability legislation (particularly for claims involving more than one jurisdiction), prompted an extensive review of current proportionate liability beginning in 2007.

In September 2011, the Standing Council on Law and Justice (**SCLJ**) (formerly the Standing Committee of Attorneys General and then replaced by the Law Crime and Community Safety Council in December 2013) released consultation draft model proportionate liability provisions and a proportionate liability regulation impact statement for public consultation.

Following further submissions, the *Revised Draft Model Proportionate Liability Provisions – 26 September 2013* (**Draft Model Provisions**) and a new *Decision Regulation Impact Statement – October 2013* (**Regulation Impact Statement**) were presented to the SCLJ in October 2013. The Regulation Impact Statement notes that stakeholders and legal commentators have identified the following two main problems with the current proportionate liability regime:[148]

- legislative inconsistencies between jurisdictions (particularly in relation to contracting out of the regime), which can lead to forum shopping
- a lack of clarity and/or certainty in the operation of particular provisions.

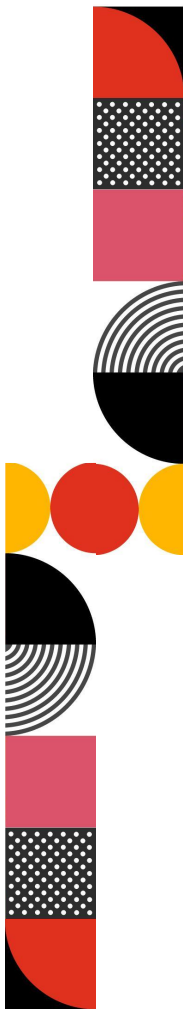
The Regulation Impact Statement considers a number of options and then recommends the introduction of uniform legislation applicable to all jurisdictions, which more narrowly defines an apportionable claim (for example as one where a failure to take reasonable care is an element of the action) and which prohibits contracting out.

The key recommended features of the proposed uniform legislation (reflected in the Draft Model Provisions), included:

- clarification that, apart from an action under the ACL for statutory misleading or deceptive conduct claims, a failure to take reasonable care must be an element of the claimant's cause of action
- 'concurrent wrongdoer' is one of two or more persons who cause the same or 'substantially or materially similar' loss or damage, even if a plaintiff has settled with them or released them from liability
- a defendant is required to provide information to a plaintiff about the identity and location of other possible concurrent wrongdoers, notify the possible concurrent wrongdoers and bears the onus of establishing a case against other possible wrongdoers
- in apportioning liability, the court must take into account the wrongdoing of a notified concurrent wrongdoer and may take into account the wrongdoing of any other concurrent wrongdoer
- in apportioning liability among concurrent wrongdoers, the court is to consider what is 'just and equitable'
- standardisation of the types of claims that are excluded from the proportionate liability regime
- if notice is given to a plaintiff of a concurrent wrongdoer, they should only be able to bring subsequent proceedings against that concurrent wrongdoer with leave of the court and caps should apply above which the plaintiff is not entitled to receive an award in subsequent proceedings
- proportionate liability legislation does not apply to arbitral tribunals or other entities capable of making a binding determination, unless they are a court or tribunal (jurisdictions may elect whether to include this provision)
- where a plaintiff settles with one concurrent wrongdoer, that concurrent wrongdoer will not be exposed to contribution claims from other concurrent wrongdoers
- contracting out is prohibited for all contracts except for an agreement by a concurrent wrongdoer to contribute to/indemnify another concurrent wrongdoer.[149]

There is a useful table in the Regulation Impact Statement which illustrates the degree to which the Draft Model Provisions represent a change to the current proportionate liability legislation in each jurisdiction.[150]

The Ministers of each jurisdiction have agreed to consider introducing the Draft Model Provisions, but there has not to date been any concrete developments in this area.



148 Page 7 of the Regulation Impact Statement.

149 See Pages 21 to 22 of the Regulation Impact Statement and also the Draft Model Provisions.

150 See Page 23 of the Regulation Impact Statement.

Annexure A

Position paper on performance liquidated damages – Power projects

Introduction

The interaction between the performance and completion conditions in an Engineering, Procurement and Construction (**EPC**) contract and the provisions for Performance Liquidated Damages (**PLDs**) payable under it will vary depending on a number of circumstances, including the size, nature and complexity of the project.

This paper outlines two suites of clauses that may be included in an EPC Contract to accommodate these situations. They are drafted for power projects, but may be relevant to other sectors, such as oil and gas and for process plant projects. Solar and wind projects will require a different regime with more of a focus on post commercial operation testing: For example, a production guarantee mechanism.

Your project requirements

Overview

This section addresses the benefits and utility of two different PLDs regimes, before discussing some of the project characteristics that might render one regime more or less suitable to your project.

Features of the simple regime

The simple regime uses a two-stage completion process whereby the Contractor does not have the ability to access the facility after the Principal assumes care, custody and control for the purposes of improving performance. Sample clauses illustrating this approach are contained in Appendix 1 (Simple regime clauses).

This regime is appropriate where:

- the planned operation of the facility is such that it is not feasible for the Principal to allow the Contractor any significant period of time beyond the date for commercial operation in which to make modifications and retest the facility
- provided the minimum performance guarantees are met, the Principal allows the Contractor to choose to retain care, custody and control so that it can improve the results of the guarantee tests whilst paying Delay Liquidated Damages (**DLDs**).

Features of the detailed regime

The detailed regime uses a three-stage completion process, incorporating a period of time after the Principal assumes control of the facility in which the Contractor may, with the Principal's approval, attempt to improve the performance of the facility whilst paying DLDs.

This regime is appropriate where:

- the Principal prefers to take possession of the facility and begin generating electricity as soon as commercial operation is achieved (effectively, in certain circumstances, as soon as the minimum performance guarantees are met)
- it is viable, even after the Principal has assumed the care, custody and control of the facility, for the Principal to allow the Contractor access to attempt to improve performance whilst paying DLDs.

Features of your project

The following questions may help decide which regime is more appropriate.

Are you building a baseload facility or a peaking facility?

Both regimes have been drafted to apply to a baseload facility, but each can easily be tailored for a peaking facility.

However, given that a peaking facility only operates during periods of high demand, it may be possible for the Principal to grant the Contractor access to the facility (after the Principal takes over the facility) without suffering undue inconvenience or expense (through lost operation time).

This may make the detailed regime more suitable to a peaking facility, especially if DLDs will run during any period that the Contractor takes the facility out of service (even if not required to generate electricity during that period).

Is there an inflexible deadline for you to begin operating the facility?

If there is an inflexible deadline by which you must begin operating the facility (such as a contractual obligation to begin selling electricity),[151] the detailed regime may be the more appropriate option.

Under the detailed regime, the Principal is better placed to take over the facility on or before the date for commercial operation (provided that the minimum performance guarantees are met), and later allow, at the Principal's discretion and convenience, the Contractor to attempt to improve the performance of the facility (during periods of low demand). The Contractor has an incentive during these periods to bring the performance of the facility to the highest possible level in order to minimise its PLDs liability. Accordingly, the Principal achieves the highest standard of plant performance without undue disruption to its operation of the facility.

Is the performance of the facility your highest priority?

If there is some flexibility in the date by which you must begin operating the facility, and the first priority is to ensure that the facility achieves the highest possible standard of performance, the simple regime may be more suitable. This regime requires commercial operation (and, in this regime, the point at which the Contractor is no longer permitted to continue work on the project) to be deferred as long as is required to meet the performance guarantees (limited only by the Contractor reaching the aggregate limit for DLDs). Under this arrangement, the Principal does not take control of the facility until the performance guarantees are met or DLDs cap out. This means the facility will be at the maximum possible level of performance by the time the Principal begins operating.



151 The performance regime for a project may also be influenced by the terms of any third party offtake agreements, particularly back-to-back arrangements for liquidated damages and other performance guarantees.

Simple regime

This section will analyse in detail the simple regime. As discussed above, it employs a two-stage completion process and does not permit the Contractor any opportunity to improve the facility's performance after the Principal assumes care, custody and control. Refer to Appendix 1 (Simple regime clauses) for the sample clauses illustrating the simple regime.

Preliminary steps

The simple regime requires several steps to be completed prior to commercial operation: mechanical completion, precommissioning, and commissioning.[152]

Mechanical completion

Mechanical completion is the stage at which the facility has been completed mechanically and structurally, within the requirements of the contract, such that the facility is able to be started. The Contractor must notify the Principal's representative when it is satisfied that the facility has reached mechanical completion. The Principal's representative must then either:

- issue a certificate of mechanical completion
- notify the Contractor of any deficiencies in the facility preventing the issue of a certificate of mechanical completion.

The Contractor must correct any defects and reapply for a certificate of mechanical completion. This procedure is repeated until the certificate of mechanical completion is issued.

Precommissioning and commissioning

Commissioning is the stage at which the facility is operated by the Contractor in a limited way for the purpose of preparing the facility for operation and for the performance tests necessary to establish commercial operation.

Prior to commissioning, the Contractor must comply with certain procedures set by the Principal (as specified in the project documentation). After these precommissioning procedures are completed, the Contractor may begin commissioning.

Commercial operation

The simple regime then sets out the steps necessary for the facility to be placed into commercial operation. Broadly, commercial operation is the point at which the facility can be operated reliably, safely and legally under the conditions it is normally expected to operate within and:

- the environmental guarantees (that is, emissions and noise) have been met
- the performance guarantees have been met[153] or PLDs paid for any shortfall in meeting such guarantees.

It is permissible for some minor items to remain outstanding at the point of commercial operation, provided that the Contractor undertakes a Programme for their proposed completion and they do not impact on the safe and efficient performance of the facility.

The steps required for achieving commercial operation are as follows.

Performance tests

After commissioning the facility, and when the Contractor is satisfied that all requirements for commercial operation have been met, it must notify the Principal's representative that the facility has achieved commercial operation.

If, during the performance tests, the performance guarantees are not met, the Contractor must make such changes, modifications and/or additions to the facility as are necessary to meet the performance guarantees. On completion of these modifications, the Contractor must notify the Principal and continue to repeat the tests until the performance guarantees are met.

This process will ordinarily continue until DLDs cap out. However, at any time between the date for commercial operation and the date of DLDs capping out, either the Contractor or the Principal may elect to stop further work on the facility. Where such an election is made, the Contractor pays PLDs in consideration of its failure to satisfy the performance guarantees.

Certificate of commercial operation

On successful completion of the performance tests, the Contractor must notify the Principal's representative that, in the Contractor's opinion, the facility has reached commercial operation.

The Principal's representative must then either:

- issue a certificate of commercial operation
- notify the Contractor of any defects preventing the facility from reaching commercial operation.

[152] Note that there will be different commissioning and testing requirements depending on the characteristics of the facility in question, including, for a gas-fired plant, whether it is single or combined cycle, and otherwise whether there are various units, staged completion or synchronisation issues.

[153] For example, both heat rate and output.

The Contractor must remedy any defects and repeat the performance tests until the Principal's representative issues a certificate of commercial operation.

The Contractor hands over care, custody and control of the facility when the Principal issues a certificate of commercial operation.

Final completion

The last stage in the simple regime is final completion, which is the point when:

- commercial operation has been achieved
- all defects and deficiencies have been remedied by the Contractor
- the defects liability period has expired.

The process for achieving final completion is as follows.

Notification

The Contractor must notify the Principal's representative that the facility has reached the stage of final completion.

Certificate of final completion

The Principal's representative must then either:

- issue a certificate of final completion
- notify the Contractor of any outstanding defects that must be remedied before final completion can be achieved.

The Contractor must remedy any defects and repeat the notification procedure until the Principal issues a certificate of final completion.

PLDs[154]

Assuming that neither party exercises their right to terminate, PLDs are payable by the Contractor upon the earlier of:

- either party electing to stop further modifications by the Contractor, provided that the date for commercial operation has passed
- DLDs capping out.

For the purposes of assessing PLDs, commercial operation will be deemed at the point at which DLDs cap out.

(Note that this discussion does not take into account any PLDs that may arise because of a failure to meet the availability guarantee).

PLDs may be payable in the following four scenarios.

Opt-out election; minimum performance guarantees not met; performance guarantees not met

This scenario will arise if, at the date for commercial operation, the minimum performance guarantees have not been met. The Contractor is obliged to continue retesting until DLDs cap out, unless, as in this scenario, either the Contractor or the Principal exercises its rights to halt further work on the facility and have the Contractor pay PLDs. At the point of that election, the minimum performance guarantees will remain unsatisfied, meaning that the performance guarantees have also not been satisfied.

Liability to pay PLDs will arise for the Contractor's failure to meet the minimum performance guarantees and to meet the performance guarantees.[155]

Opt-out election; minimum performance guarantees met; performance guarantees not met

This situation will arise as in the paragraph above, except that at the date for commercial operation the minimum performance guarantees may or may not have been met, and, in any event, at the point of the Contractor or the Principal electing not to continue modification, the Contractor will have achieved the minimum performance guarantees.

Accordingly, the Contractor's liability to pay PLDs will arise only in respect of the failure to meet the performance guarantees.

DLDs cap out; minimum performance guarantees not met; performance guarantees not met

This scenario will arise where the Contractor has failed to meet the minimum performance guarantees during the performance tests and continued modification and retesting by the Contractor fails to improve the facility for it to meet the minimum performance guarantees before DLDs cap out.

Liability to pay PLDs will arise for the Contractor's failure to meet the minimum performance guarantees and to meet the performance guarantees.

DLDs cap out; minimum performance guarantees met; performance guarantees not met

This scenario will arise where the performance tests demonstrate that the minimum performance guarantees have been met, but the performance guarantees have not. The Contractor is accordingly obliged to continue modifications and retesting. PLDs will become payable if, at the point DLDs cap out, the Contractor has failed to improve performance to meet the performance guarantees.

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154 Depending on the nature of the project and other commercial considerations, PLDs may not always be suitable compensation for a failure to achieve the minimum performance guarantees. Other options available to the Principal can include a right to reject the facility and buy-down (at a price determined by a pre-agreed valuation formula) or the Principal may wish to terminate the contract and engage others to complete the facility at the Contractor's cost.

155 Note that there may be differing rates of PLDs. PLDs for a failure to meet the minimum performance guarantees may be higher than those payable for a failure to achieve the Performance Guarantees.

Detailed regime

This section will discuss the operation and function of the detailed regime. As stated earlier, the detailed regime establishes a three-stage completion process, incorporating a period of time in which the Contractor may, with the Principal's approval, attempt to improve the performance of the facility. This period of time occurs after the Principal certifies commercial operation and takes control of the facility.

Sample clauses illustrating the detailed regime are included in Appendix 2 (Detailed regime clauses).

Preliminary steps

Under the detailed regime, several steps must be completed to achieve commercial operation.

Mechanical completion, precommissioning and commissioning

Under the detailed regime, the concepts of mechanical completion, precommissioning and commissioning are identical to those under the simple regime (see above).

Commercial operation

After mechanical completion, precommissioning and commissioning, the detailed regime then specifies certain steps that are required for the facility to be placed into commercial operation. Similar to the notion of commercial operation in the simple regime, commercial operation is the point at which the facility can be operated reliably, safely and legally under the conditions it is normally expected to operate within and:

- the environmental guarantees have been met
- the minimum performance guarantees have been satisfied
- One of:
  - the performance guarantees have been met
  - the Contractor has paid PLDs in consideration of its failure to meet the performance guarantees
  - the Contractor has elected to utilise the subsequent testing period in an attempt to meet the performance guarantees post-commercial operation and has given security for the PLDs that would otherwise be payable.

It is permissible for some minor items to remain outstanding at the point of commercial operation, provided that the Contractor provides a Programme for their proposed completion.

After the preliminary steps are completed, the procedures that must be followed to achieve commercial operation are as follows:

Performance tests

Once the Contractor is satisfied that all requirements for commercial operation have been met, the Contractor must notify the Principal's representative. The performance tests must then take place.

If, after the performance tests are completed, the minimum performance guarantees have not been met, the Contractor must, at its own expense, make such changes, modifications or additions as may be required to meet the minimum performance guarantees. When the modifications are completed, the Contractor must notify the Principal and continue to repeat the overall performance test until the minimum performance guarantees are met.

Otherwise, if, after the performance tests are completed, the:

- performance guarantees have been met
- minimum performance guarantees have been met and either:
  - the Contractor elects to pay PLDs in lieu of meeting the performance guarantees
  - if DLDs have not capped out, the Contractor elects to give security and exercise its rights to utilise the subsequent testing period, the Contractor must notify the Principal's representative that the facility has reached commercial operation.

Certificate of commercial operation

The Principal must either:

- issue a certificate of commercial operation (effectively certifying that the minimum performance guarantees have been met)
- notify the Contractor of any defects or deficiencies that prevent the facility from reaching commercial operation.

The Contractor must remedy any defects and again notify the Principal that the facility is ready for commercial operation. This process must be repeated until the Principal issues a certificate of commercial operation.

When the Principal issues the certificate of commercial operation, care, custody and control of the facility is handed to the Principal. Note that the Principal has the discretion to issue a certificate of commercial operation at any time (notwithstanding that the requirements for issuing a certificate of commercial operation have not been met).

At this point, if the minimum performance guarantees have been met, but the performance guarantees have not, and the Contractor has elected to pay PLDs rather than attempt to improve the facility's performance, the PLDs must be paid.

Alternately, if the minimum performance guarantees have been met, but the performance guarantees have not, and the Contractor has provided the Principal with security for the PLDs (in the form of payment or a bank guarantee), the subsequent testing period commences.

Subsequent testing period[156]

The subsequent testing period is a 60-day period after commercial operation in which, if the performance guarantees have not been met and the Contractor elects to utilise the subsequent testing period, the Contractor may request access to the facility to perform modifications and otherwise seek to improve performance (despite the fact that care, custody and control of the facility has passed to the Principal).

During the subsequent testing period, the Contractor may at any time:

- request the facility to be taken out of service
- at its own expense, make changes, modification or additions to the facility in an attempt to meet the performance guarantees
- notify the Principal upon completion of any changes or modifications
- continue to repeat the overall performance test.

The Principal has an absolute discretion to refuse or reschedule the Contractor's request to take the facility out of service. During periods where the facility is taken out of service, the Contractor assumes sole and absolute responsibility for the care, custody and control of the facility and bears the risk of loss or damage to it.

Final commercial operation

Where the Contractor has failed to meet the performance guarantees at the point of commercial operation and elects to utilise the subsequent testing period, a further stage of completion is required (Final Commercial Operation).

Final Commercial Operation is reached on the earliest of:

- the date DLDs cap out
- the expiration of the subsequent testing period
- the date on which the Principal issues the certificate of final completion.

There are two stages to the achievement of Final Commercial Operation.

Notification

The Contractor must notify the Principal's representative that it believes the facility has reached Final Commercial Operation.

Certification of final commercial operation

The Principal's representative must either:

- issue a certificate of Final Commercial Operation
- notify the Contractor of any defects preventing the facility from reaching Final Commercial Operation (effectively, any defect causing the facility to no longer satisfy the minimum performance guarantees or another compulsory condition).

The Contractor must remedy any defects and again notify the Principal's representative that the facility has reached Final Commercial Operation. This procedure must be repeated until the Principal's representative issues a certificate of Final Commercial Operation.

Final completion

The final completion procedure is identical under both the simple and detailed regimes (see above).

PLDs

PLDs become payable under the detailed regime at the point of:

- if the minimum performance guarantees are not met (and thus commercial operation is not achieved) before DLDs cap outcommercial operation
- where the subsequent testing period is utilised, Final Commercial Operation.

(Note that this discussion does not take into account any PLDs that may arise because of a failure to meet the availability guarantee.)

The following sections set out the PLDs that will be payable in the three possible scenarios.

DLDs cap out; minimum performance guarantees not met; performance guarantees not met

This scenario will arise either where the Contractor:

- does not reach the point of carrying out performance tests on the facility before DLDs cap out and overall performance tests at that point reveal that the minimum performance guarantees have not been met
- has failed to meet the minimum performance guarantees at the point of the performance tests and continued modification and retesting fails to improve the facility for it to meet the minimum performance guarantees before DLDs cap out.

In this case, liability to pay PLDs will arise in respect of the failure both to meet the minimum performance guarantees and to meet the performance guarantees.

Commercial operation; minimum performance guarantees met; performance guarantees not met

This scenario will arise only where the performance tests demonstrate that the minimum performance guarantees have been met, but the performance guarantees have not been met and the Contractor elects to immediately pay PLDs in consideration of its failure to meet the performance guarantees. PLDs will become payable in this scenario as soon as the Contractor makes such an election.

[156] During this period, the Contractor is responsible for the cost of fuel, water and all other consumables necessary for the additional testing.

Final commercial operation: minimum performance guarantees met, performance guarantees not met.

This scenario will arise where the performance tests demonstrate that the minimum performance guarantees have been met, but the performance guarantees have not been met and the Contractor applies for commercial operation and elects to utilise the subsequent testing period.

In this scenario, the Contractor must secure its potential PLDs liability (as at commercial operation) by either:

- paying the PLDs that would be payable at commercial operation (for the failure to meet the performance guarantees)
- providing a bank guarantee to the Principal for the same amount.

At the point of Final Commercial Operation, PLDs will crystallise and:

- if the Contractor has met the performance guarantees, the money paid or security will be refunded or released, less an offset for the period of reduced performance between commercial operation and Final Commercial Operation
- if the Contractor has improved the performance of the facility, but has not met the performance guarantees, a portion of the money paid or security will be refunded or released, proportionate with the increase in performance, less an offset for the period of reduced performance between commercial operation and Final Commercial Operation
- if the performance of the facility is the same as or worse than it was at commercial operation, the Principal will retain the PLDs or cash the guarantee and the Contractor will be liable to pay to the Principal an amount equal to the difference between the PLDs now payable for the deficiency in performance and the money or guarantee already given by the Contractor.



Annexure 1

Simple regime clauses

Precommissioning and commissioning

Mechanical completion

(a) As soon as the facility, in the opinion of the Contractor, reaches the stage of Mechanical Completion, the Contractor must give a notice to the Owner's representative.

(b) The Owner's representative must, promptly, and no later than five business days after receipt of the Contractor's notice under clause 1.1(a), either issue a Certificate of Mechanical Completion stating that the facility has reached Mechanical Completion or notify the Contractor of any defects and/or deficiencies.

(c) If the Owner's representative notifies the Contractor of any defects and/or deficiencies, the Contractor must then correct those defects and/or deficiencies and the procedures described in clauses 1.1(a) and (b) must be repeated until the Owner's representative issues a Certificate of Mechanical Completion.

Precommissioning

The Contractor must comply with the Owner's requirements and procedures in relation to Precommissioning as set out in the schedule of technical specification.

Commissioning

As soon as all works in respect of Precommissioning are completed the Contractor must notify the Owner's representative in writing that the facility is ready for the commissioning tests.

Requirements and procedures

The Contractor must comply with the Owner's requirements and procedures in relation to Commissioning and the performance of the commissioning tests as set out in the schedule of technical specification.

Performance tests, commercial operation and final completion

(a) After the initial testing is completed, and as soon as the facility, in the opinion of the Contractor, satisfies all the requirements for Commercial Operation (other than the passing of the Performance Tests), the Contractor must notify the Owner's representative in writing that the facility is ready for the Performance Tests.

(b) Each Performance Test must be completed at the time and in accordance with the procedures specified in the schedule of tests.

(c) The Contractor acknowledges and agrees that, despite any other provision of this contract, no partial or entire use or generation of electricity or occupancy of the site, the Works or the facility as a whole by the Owner, whether prior to, during or after the Performance Tests or otherwise, in any way constitutes an acknowledgment by the Owner that Commercial Operation has occurred, nor does it operate to release the Contractor from any of its warranties, obligations or liabilities under or in connection with this contract.

Commercial operation

(a) As soon as the facility has passed the Performance Tests the Contractor must notify the Owner's representative in writing that the facility has, in the Contractor's opinion, reached Commercial Operation. That notice must, if applicable, also include the Contractor's list of minor outstanding items that in its view meet the requirements of paragraph (k) of the definition of Commercial Operation and a Programme for expeditiously completing those minor outstanding items.

(b) The Owner's representative must promptly, and no later than five days after receipt of the Contractor's notice under clause 2.2(a), either issue a Certificate of Commercial Operation stating the date on which the facility has reached Commercial Operation or notify the Contractor in writing of any defects and/or deficiencies that prevent the facility from achieving Commercial Operation.

(c) If the Owner's representative notifies the Contractor of any such defects and/or deficiencies, the Contractor must then remedy those defects and/or deficiencies and the procedures described in clauses 2.2(a) and (b) must be repeated until the Owner issues a Certificate of Commercial Operation.

(d) Upon the issue of the Certificate of Commercial Operation, the Contractor must hand over care, custody and control of the facility to the Owner.

(e) Notwithstanding that all the requirements for the issuing of a Certificate of Commercial Operation have not been met, the Owner may at any time, in its absolute, sole and unfettered discretion, issue a Certificate of Commercial Operation. The issue of a Certificate of Commercial Operation in accordance with this clause 2.2(e) will waive the requirement of paragraph (d) of the definition of Commercial Operation but will not operate as an admission that all the other requirements of Commercial Operation have been met, and does not prejudice any of the Owner's rights, including the right to require the Contractor to satisfy all these requirements, nor does it release the Contractor from any of its warranties, obligations or liabilities under or in connection with this contract.

Final completion

(a) As soon as the facility, in the opinion of the Contractor, reaches the stage of Final Completion, the Contractor must give a written notice to the Owner's representative.

(b) The Owner's representative must, promptly, and no later than five days after receipt of the Contractor's notice under clause 2.3(a), either issue a Certificate of Final Completion stating that the facility has reached Final Completion or notify the Contractor in writing of any defects and/or deficiencies that must be remedied before Final Completion can be achieved.

(c) If the Owner's representative notifies the Contractor of any outstanding defects and/or deficiencies, the Contractor must then remedy those defects and/or deficiencies and the procedures described in clauses 2.3(a) and (b) must be repeated until the Owner issues a Certificate of Final Completion.



Performance guarantees

Performance guarantees

(a) The Contractor guarantees that the facility as a whole and all sections thereof will meet the:

  (i) Performance Guarantees

  (ii) Environmental Guarantees

  (iii) as specified in the schedule of performance guarantees and the schedule of tests.

(b) The Contractor agrees that the Environmental Guarantees are absolute guarantees, the meeting of which is a condition precedent to achieving Commercial Operation.

Performance guarantees not met – Retesting

If for reasons not attributable to the Owner, either or both of the Performance Guarantees are not met during the same Performance Test, the Contractor must:

(a) at its cost and expense make changes, modifications and/or additions to the facility or any part as may be necessary to meet the Performance Guarantees

(b) notify the Owner upon completion of the necessary changes, modifications and/or additions

(c) subject to the Owner's rights under clauses 2.2(e) and 3.5 and 3.14, continue to repeat the Performance Test until the Performance Guarantees have been met during the same Performance Test.

Minimum Performance Guarantees not met – PLDs

Subject to clause 2.2(e), if for reasons not attributable to the Owner, the Contractor does not meet one or more of the minimum performance guarantees by the date it has incurred or is liable for Delay Liquidated Damages up to the aggregate liability specified in the schedule of delay liquidated damages, the Owner may require the Contractor to pay:

(a) if the Minimum Net Electrical Output Performance Guarantee has been met (but the net electrical output performance guarantee has not been met), Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages

(b) if the Minimum Net Electrical Output Performance Guarantee has not been met:

  (i) an amount equal to the amount the Contractor would have been liable for if the actual rated net output of the facility was equal to 95.0% of the net electrical output performance guarantee as specified in the schedule of performance liquidated damages

  (ii) Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

(c) if the Minimum Net Heat Rate Performance Guarantee has been met (but the net heat rate performance guarantee has not been met), Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages

(d) if the Minimum Net Heat Rate Performance Guarantee has not been met:

  (i) an amount equal to the amount the Contractor would have been liable for if the actual net heat rate of the facility was equal to 105.0% of the net heat rate performance guarantee as specified in the schedule of performance liquidated damages

  (ii) Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

Performance guarantees not met – PLDs

If for reasons not attributable to the Owner, the Contractor has met the minimum performance guarantees but does not meet one or more of the Performance Guarantees by the date it has incurred or is liable for Delay Liquidated Damages up to the aggregate liability specified in the schedule of delay liquidated damages, the Contractor is liable to pay Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

Performance guarantees not met after date for commercial operation – Opt out

(a) Despite clauses 3.3 and 3.4, the Contractor may at any time after the Date for Commercial Operation elect to pay Performance Liquidated Damages in respect of the failure to meet either or all of the Performance Guarantees (for reasons not attributable to the Owner), provided the minimum performance guarantees and the Environmental Guarantees have been met.

(b) Despite clauses 3.3 and 3.4, the Owner may at any time after the Date for Commercial Operation require the Contractor to pay Performance Liquidated Damages in respect of the failure to meet any or all of the Performance Guarantees (for reasons not attributable to the Owner), provided the minimum performance guarantees and the Environmental Guarantees have been met.

Satisfaction of performance guarantees

The payment of Performance Liquidated Damages under clause 3 will be in satisfaction of the relevant Performance Guarantee or Performance Guarantees.

Environmental guarantees

If the Contractor has met the Performance Guarantees or the minimum performance guarantees, as the case may be, but does not, for reasons not attributable to the Owner, during the same Overall Performance Test, meet the Environmental Guarantees, the performance of the facility may, at the Contractor's option, be derated to a level not below the Minimum Performance Guarantee levels, to enable the Emissions Guarantees to be achieved. If the Contractor elects to derate the performance of the facility, the Contractor must pay Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages for such derated performance.

Availability guarantee

The Contractor guarantees that the facility either in whole or in part will operate at the guaranteed availability for a period of 12 months from not later than two months after the Date of Commercial Operation.

Availability – PLDs

If the Availability Guarantee is not achieved, the Contractor must pay Performance Liquidated Damages as specified in the schedule of performance liquidated damages.

Aggregate liability

The aggregate liability of the Contractor for Performance Liquidated Damages under clause 3 will not exceed the amount calculated in accordance with the schedule of performance liquidated damages.

Invoicing

Performance Liquidated Damages must be invoiced by the Owner and payment must be made by the Contractor within 15 days of the date of the invoice. At the expiration of those 15 days, the amount involved is, if not paid, a debt due and payable to the Owner by the Contractor.

Fair and reasonable pre-estimate

The parties agree that the Performance Liquidated Damages in the schedule of performance liquidated damages are a fair and reasonable pre-estimate of the damages likely to be sustained by the Owner as a result of the Contractor's failure to meet the minimum performance guarantees and/or the Performance Guarantees.

No relief

(a) The payment of Performance Liquidated Damages does not in any way relieve the Contractor from any of its obligations to complete the Works or from any of its warranties, obligations or liabilities under or in connection with this contract.

(b) Without prejudice to clause 3.13(a), the payment of Performance Liquidated Damages under this clause 3 is in addition to any liability of the Contractor for Delay Liquidated Damages.

Rights at law

If this clause 3 (or any part) is found for any reason to be void, invalid or otherwise inoperative so as to disentitle the Owner from claiming Performance Liquidated Damages, the Owner is entitled to claim against the Contractor for damages at law for the Contractor's failure to meet the Performance Guarantees. Such damages must not exceed the amounts specified in the schedule of damages at law.

No benefit

The Contractor is not entitled to the benefit of the exclusion of liability for consequential loss under this contract in any claim for damages at law by the Owner against the Contractor pursuant to clause 3.14.

Duplicate damages

Nothing in this clause 3 entitles the Owner to claim duplicate damages in respect of the failure of the Contractor to meet the Performance Guarantees, the minimum performance guarantees or the Availability Guarantee.

Definitions

Availability Guarantee means the guarantee specified as the 'Availability Guarantee' in the [schedule of performance guarantees].

Availability Test means the test described as the Availability Test in the [schedule of tests].

Certificate of Commercial Operation means the certificate issued by the Owner under clause 2.2 in the form set out in the [schedule of forms of certificates].

Certificate of Final Completion means the certificate issued under clause 2.3 in the form set out in the [schedule of forms of certificates].

Certificate of Mechanical Completion means the certificate issued under clause 1.1(b) in the form set out in the [schedule of forms of certificates].

Commercial Operation means the stage of the Works when the following has occurred:

(a) the Contractor has provided copies of the draft operation and maintenance manual

(b) the Emissions Guarantee Test has been passed

(c) the Noise Guarantee has been met

(d) the Minimum Performance Guarantees have been met

(e) the Performance Guarantees have been met or, where applicable, Performance Liquidated Damages have been paid

(f) the facility is capable of being operated reliably, safely and efficiently under all anticipated or likely operational conditions

(g) the Contractor has provided the Spare Parts required to be provided by the Date for Commercial Operation

(h) the facility is in a condition which allows the Owner to comply with all laws relating to its operation

(i) all documents and other information in respect of the facility required under this contract have been supplied to the Owner or the Owner's representative

(j) all government approvals to be obtained by the Contractor under the contract and which are necessary for the operation of the facility, and to the full extent permitted by law, have been transferred (to the extent necessary and/or permitted at law) to the Owner or the Owner's nominee

(k) the facility is complete in all respects other than minor items that in the reasonable opinion of the Owner's representative will not prejudice (either by not being completed or as a result of the work needed to complete them), the ability of the Owner to operate the facility legally, safely, reliably and efficiently.

Commissioning means the operation of the facility, or any part, by the Contractor following Precommissioning in accordance with the schedule of project technical requirements [not included], which operation is to be carried out by the Contractor as provided in clause 1.4, for the purpose of preparing the facility for operation and the carrying out of the Performance Tests.

Date for Commercial Operation means, in respect of the facility, the date specified in the [schedule of guaranteed dates], as may be varied in accordance with the terms of the contract.

Date of Commercial Operation means the date specified in the Certificate of Commercial Operation.

Defects Liability Period means the period of 12 months from:

(a) in relation to the facility as a whole, the Date of Commercial Operation

(b) in relation only to where a part or parts of the facility are repaired, replaced or made good, the date of commencement in accordance with the contract as the case may be.

Delay Liquidated Damages means the liquidated damages for delay specified in the relevant section of the [schedule of delay liquidated damages].

Emissions Guarantee means the guarantee specified in the [schedule of performance guarantees], which is an absolute guarantee and the meeting of which is a condition precedent to achieving Commercial Operation.

Emissions Guarantee Tests means the tests specified as the emissions guarantee tests in the [schedule of tests].

Environmental Guarantees means the Emissions Guarantee and the Noise Guarantee as specified in the [schedule of performance guarantees].

Final Completion means the stage of the Works when:

(a) Commercial Operation has been achieved

(b) all defects and/or deficiencies have been satisfactorily remedied

(c) the Defects Liability Period has expired.

Mechanical Completion means that the facility has been completed mechanically and structurally in accordance with the [schedule of project technical requirements] and the other requirements of the contract such that in the reasonable opinion of the Owner's representative the facility is substantially completed and able to operate safely, reliably and efficiently and the facility is ready for Precommissioning and Commissioning.

Minimum Net Electrical Output Performance Guarantee means the minimum net output performance level specified in the schedule of performance guarantees.

Minimum Net Heat Rate Performance Guarantee means the minimum net heat rate performance level specified in the schedule of performance guarantees.

Minimum Performance Guarantees means the Minimum Net Heat Rate Performance Guarantee and the Minimum Net Electrical Output Performance Guarantee.

Noise Guarantee means the guarantee specified as the 'Noise Guarantee' in the [schedule of performance guarantees], which is an absolute guarantee and the meeting of which is a condition precedent to achieving Commercial Operation and Final Commercial Operation.

Noise Guarantee Tests means the tests specified as the noise guarantee tests in the [schedule of tests].

Overall Performance Test means a test in which the Performance Guarantees and the Environmental Guarantees are measured simultaneously.

Performance Guarantees means the performance guarantees to be met in relation to Commercial Operation as set out in the [schedule of performance guarantees] but does not include the Environmental Guarantees.

Performance Liquidated Damages means the liquidated damages for underperformance of the facility as specified in the [schedule of performance liquidated damages].

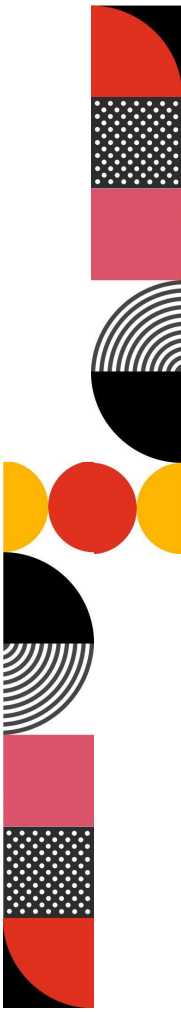
Performance Tests means the tests described as Performance Tests in the [schedule of tests].

Precommissioning means the testing, checking and other works specified in the [schedule of project technical requirements] to be performed by the Contractor in preparation for Commissioning.

Spare Parts means the spare parts the Contractor is obliged to provide pursuant to the contract that must, as a minimum, comprise the parts listed in the [schedule of project technical requirements].

Works means all the equipment to be supplied and the whole of the work and services to be performed by the Contractor under the contract in accordance with the contract documents and as further described in the schedule of project technical requirements and includes any variation.





Annexure 2

Detailed regime clauses

1. Precommissioning and commissioning

1.1 Mechanical completion

(a) As soon as the facility, in the opinion of the Contractor, reaches the stage of Mechanical Completion, the Contractor must give a notice to the Owner's representative.

(b) The Owner's representative must, promptly, and no later than five business days after receipt of the Contractor's notice under clause 1.1(a), either issue a Certificate of Mechanical Completion stating that the facility has reached Mechanical Completion or notify the Contractor of any defects and/or deficiencies.

(c) If the Owner's representative notifies the Contractor of any defects and/or deficiencies, the Contractor must then correct those defects and/or deficiencies and the procedures described in clauses 1.1(a) and (b) must be repeated until the Owner's representative issues a Certificate of Mechanical Completion.

1.2 Precommissioning

The Contractor must comply with the Owner's requirements and procedures in relation to Precommissioning as set out in the schedule of technical specification.

1.3 Commissioning

As soon as all works in respect of Precommissioning are completed, the Contractor must notify the Owner's representative in writing that the facility is ready for the Commissioning Tests.

1.4 Requirements and procedures

The Contractor must comply with the Owner's requirements and procedures in relation to Commissioning and the performance of the Commissioning Tests as set out in the schedule of technical specification.

2. Performance tests, commercial operation and final completion

2.1 Performance tests

(a) After the initial testing is completed, and the Contractor is satisfied that all requirements for Commercial Operation (other than the passing of the Performance Tests) have been met, the Contractor must notify the Owner's representative in writing that the facility is ready for the Performance Tests.

(b) Each Performance Test must be completed at the time and in accordance with the procedures specified in the schedule of tests.

(c) The Contractor acknowledges and agrees that, despite any other provision of this contract, no partial or entire use or generation of electricity or occupancy of the site, the Works or the facility as a whole by the Owner, whether prior to, during or after the Performance Tests or otherwise, in any way constitutes an acknowledgment by the Owner that Commercial Operation has occurred, nor does it operate to release the Contractor from any of its warranties, obligations or liabilities under or in connection with this contract.

2.2 Commercial operation

(a) After the Performance Tests are completed and the:

(b) Performance Guarantees have been met.

(c) Minimum Performance Guarantees have been met and the Contractor elects to pay the applicable Performance Liquidated Damages in accordance with clause 3.4.

(d) Minimum Performance Guarantees have been met and provided the Contractor has not incurred Delay Liquidated Damages equal to or in excess of the amount specified in section 2 of the schedule of delay liquidated damages, the Contractor elects to exercise its rights under clause 2.3 and provide security or pay the applicable Performance Liquidated Damages in accordance with clause 3.4.

The Contractor must notify the Owner's representative in writing that the facility has, in the Contractor's opinion, reached Commercial Operation. That notice must, if applicable, also include the Contractor's list of minor outstanding items that in its view meet the requirements of paragraph (j) of the definition of Commercial Operation and a Programme for expeditiously completing those minor outstanding items.

(e) The Owner's representative must promptly, and no later than five days after receipt of the Contractor's notice under clause 2.2(a), either issue a Certificate of Commercial Operation stating the date on which the facility has reached Commercial Operation or notify the Contractor in writing of any defects and/or deficiencies that prevent the facility from achieving Commercial Operation.

(f) If the Owner's representative notifies the Contractor of any such defects and/or deficiencies, the Contractor must then remedy those defects and/or deficiencies and the procedures described in clauses 2.2(a) and (b) must be repeated until the Owner issues a Certificate of Commercial Operation.

(g) Upon the issue of the Certificate of Commercial Operation, the Contractor must hand over care, custody and control of the facility to the Owner.

(h) Notwithstanding that all the requirements for the issuing of a Certificate of Commercial Operation have not been met, the Owner may at any time, in its absolute, sole and unfettered discretion, issue a Certificate of Commercial Operation. The issue of a Certificate of Commercial Operation in accordance with this clause 2.2(e) will waive the requirement of paragraph (d) of the definition of Commercial Operation but will not operate as an admission that all the other requirements of Commercial Operation have been met, and does not prejudice any of the Owner's rights, including the right to require the Contractor to satisfy all these requirements, nor does it release the Contractor from any of its warranties, obligations or liabilities under or in connection with this contract.

2.3 Subsequent testing period

If the Contractor has elected under clause 2.2(a)(iii) to exercise its rights under this clause 2.3, the Contractor may, at any time during the Subsequent Testing Period:

(a) request the facility or any part of the facility be taken out of Service

(b) at its cost and expense make changes, modifications and/or additions to the facility or any part as may be necessary to meet the Performance Guarantees

(c) notify the Owner upon completion of the necessary changes, modifications and/or additions

(d) continue to repeat the Overall Performance Test, in order to meet the Performance Guarantees.

The Owner may in its absolute discretion refuse or reschedule the Contractor's request to take the facility or any part of the facility out of Service or otherwise modify or adapt the facility or any part of the facility as a result of operational requirements. The Contractor is solely and absolutely responsible for ensuring the facility or any part of the facility returns to Service and operates in accordance with the requirements of this contract after it is taken out of Service pursuant to this clause 2.3. In addition, the Contractor is responsible for the care, custody and control of the facility and bears the risk of loss or damage to the facility or part of the facility taken out of Service pursuant to this clause 2.3 until the facility or any such part is returned to Service.

During the Subsequent Testing Period, the Owner agrees that the Contractor is not liable for Delay Liquidated Damages during any scheduled outage.

2.4 Final commercial operation

(a) The Contractor must notify the Owner's representative in writing that the facility has, in the Contractor's opinion, reached Final Commercial Operation, on:

(i) the date the Contractor has incurred liability for Delay Liquidated Damages equal to the amount specified in the Schedule of Delay Liquidated Damages

(ii) the expiration of the Subsequent Testing Period

(iii) at any other time during the Subsequent Testing Period.

(b) The Owner's representative must promptly, and no later than five days after receipt of the Contractor's notice under clause 2.4(a), either issue a Certificate of Final Commercial Operation stating the date on which the facility has reached Final Commercial Operation or notify the Contractor in writing of any defects and/or deficiencies that prevent the facility from achieving Final Commercial Operation.

(c) If the Owner's representative notifies the Contractor of any such defects and/or deficiencies, the Contractor must then remedy those defects and/or deficiencies and the procedures described in clauses 2.4(a) and (b) must be repeated until the Owner issues a Certificate of Final Commercial Operation.

2.5 Final completion

(a) As soon as the facility, in the opinion of the Contractor, reaches the stage of Final Completion the Contractor must give a written notice to the Owner's representative.

(b) The Owner's representative must, promptly, and no later than five days after receipt of the Contractor's notice under clause 2.5(a), either issue a Certificate of Final Completion stating that the facility has reached Final Completion or notify the Contractor in writing of any defects and/or deficiencies that must be remedied before Final Completion can be achieved.

(c) If the Owner's representative notifies the Contractor of any outstanding defects and/or deficiencies, the Contractor must then remedy those defects and/or deficiencies and the procedures described in clauses 2.5(a) and (b) must be repeated until the Owner issues a Certificate of Final Completion.



3. Performance guarantees

3.1 Trial runs, performance guarantees, environmental guarantees

(a) The Contractor guarantees that the facility as a whole and all parts will pass the trial runs and meet the:

(i) Performance Guarantees

(ii) Environmental Guarantees, as specified in the Schedule of Performance Guarantees and the Schedule of Tests.

(b) The Contractor agrees that the meeting of the Environmental Guarantees and the passing of each trial run are absolute guarantees and requirements, the meeting and passing of which are conditions precedent to achieving Commercial Operation.

3.2 Minimum performance guarantees not met – Retesting

If, for reasons not attributable to the Owner, either or both of the Minimum Performance Guarantees are not met during the same Overall Performance Test, the Contractor must:

(a) at its cost and expense make changes, modifications and/or additions to the facility or any part as may be necessary to meet the Minimum Performance Guarantees

(b) notify the Owner upon completion of the necessary changes, modifications and/or additions

(c) subject to the Owner's rights under clauses 2.2(e) and 3.3 and 3.13, continue to repeat the Overall Performance Test until the Minimum Performance Guarantees have been met during the same Overall Performance Test.

Subject to clause 3.3, nothing in this clause 3.2 derogates from the Contractor's obligation to meet the Performance Guarantees.

3.3 Minimum performance guarantees not met – PLDs

Subject to clause 2.2(e), if for reasons not attributable to the Owner, the Contractor does not meet one or more of the Minimum Performance Guarantees by the date it has incurred or is liable for Delay Liquidated Damages up to the aggregate liability specified in the schedule of delay liquidated damages, the Owner may require the Contractor to pay:

(a) If the Minimum Net Electrical Output Performance Guarantee has been met (but the net electrical output performance guarantee has not been met): Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

(b) If the Minimum Net Electrical Output Performance Guarantee has not been met:

(i) an amount equal to the amount the Contractor would have been liable for if the actual rated net output of the facility was equal to 95.0% of the net electrical output performance guarantee as specified in the schedule of performance liquidated damages

(ii) Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

(c) If the Minimum Net Heat Rate Performance Guarantee has been met but the net heat rate performance guarantee has not been met: Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

(d) If the Minimum Net Heat Rate Performance Guarantee has not been met:

(i) an amount equal to the amount the Contractor would have been liable for if the actual net heat rate of the facility was equal to 105.0% of the net heat rate performance guarantee as specified in the schedule of performance liquidated damages

(ii) Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

3.4 PLDs – Commercial operation

If the Performance Guarantees have not been met, but the Minimum Performance Guarantees have been met, the Contractor may apply for Commercial Operation in accordance with clause 2.2 provided all the requirements for Commercial Operation have been satisfied and it:

(a) pays to the Owner Performance Liquidated Damages calculated in accordance with the Schedule of Performance Liquidated Damages

(b) elects under clause 2.2(a)(iii) to exercise its rights under clause 2.3 and:

(i) pays to the Owner Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages that would be payable if the Contractor's liability for Performance Liquidated Damages crystallised on the day the Contractor applied for Commercial Operation

(ii) provides the Owner with an irrevocable and unconditional bank guarantee in a form and from a financial institution approved by the Owner, in its absolute discretion, for an amount equal to the Performance Liquidated Damages that would be payable if the Contractor's liability for Performance Liquidated Damages crystallised on the day the Contractor applied for Commercial Operation.

If the Contractor has met the Performance Guarantees or the Minimum Performance Guarantees, as the case may be, but does not, for reasons not attributable to the Owner, during the same Overall Performance Test, meet the Environmental Guarantee, the performance of the facility may, at the Contractor's option, be derated to a level not below the Minimum Performance Guarantee levels, to enable the Emissions Guarantees to be met. If the Contractor elects to derate the performance of the facility, the Contractor must pay Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages for such derated performance.

3.5 PLDs – Final commercial operation

(a) If the Contractor elects under clause 2.2(a)(iii) to exercise its rights under clause 2.3, on:

(i) the date the Contractor has incurred liability for Delay Liquidated Damages equal to the amount specified in the schedule of delay liquidated damages

(ii) the expiration of the Subsequent Testing Period

(iii) the date nominated by the Contractor under clause 2.3(a)(iii), the Contractor's liability for Performance Liquidated Damages will crystallise and the Contractor is liable for Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages.

the Contractor's liability for Performance Liquidated Damages pursuant to clause 3.5(a) is calculated by reference to the highest level at which the facility performed during the Overall Performance Test while still meeting the Environmental Guarantees.

(b) If the amount calculated under clause 3.5(a) is greater than the security provided by, or the Performance Liquidated Damages paid by, the Contractor under clause 3.4(b)(i) or clause 3.4(b)(ii), as the case may be, then the Contractor must pay to the Owner the difference.

(c) If the amount calculated under clause 3.5(a) is less than the security provided by, or the Performance Liquidated Damages paid by, the Contractor under clause 3.4(b)(i) or clause 3.4(b)(ii) as the case may be, the Owner must either:

(i) refund the Contractor from the monies paid pursuant to clause 3.4(b)(i) so that the net amount retained by the Owner is equal to amount to Performance Liquidated Damages the Contractor is liable for under clause 3.5(a)

(ii) release the remainder of the bank guarantee provided pursuant to clause 3.4(b)(ii) after cashing the guarantee for an amount equal to the amount of Performance Liquidated Damages the Contractor is liable for under clause 3.5(a).

(d) The Contractor must, in addition to its obligation to pay Performance Liquidated Damages under clauses 3.4(b)(i) and 3.5(c) or provide security under clause 3.4(b)(ii) as the case may be, pay Performance Liquidated Damages calculated in accordance with the schedule of performance liquidated damages for the reduced performance of the facility during the period between Commercial Operation and Final Commercial Operation, less the number of days the facility is out of Service.

3.6 Availability guarantee

The Contractor guarantees that the facility either in whole or in part will operate at the guaranteed availability for a period of 12 months from not later than two months after the Date of Commercial Operation.

3.7 Availability – PLDs

If the Availability Guarantee is not achieved, the Contractor must pay Performance Liquidated Damages as specified in the schedule of performance liquidated damages.

3.8 Aggregate liability

The aggregate liability of the Contractor for Performance Liquidated Damages under clause 3 will not exceed the amount calculated in accordance with the schedule of performance liquidated damages.

3.9 Satisfaction of performance guarantees

The payment of Performance Liquidated Damages under clause 3 will be in satisfaction of the relevant Performance Guarantee.

3.10 Invoicing

Performance Liquidated Damages must be invoiced by the Owner and payment must be made by the Contractor within 15 days of the date of the invoice. At the expiration of those 15 days, the amount involved is, if not paid, a debt due and payable to the Owner by the Contractor.

3.11 Fair and reasonable pre-estimate

The parties agreed that the Performance Liquidated Damages in the schedule of performance liquidated damages are a fair and reasonable pre-estimate of the damages likely to be sustained by the Owner as a result of the Contractor's failure to meet the Minimum Performance Guarantees and/or the Performance Guarantees.

3.12 No relief

(a) The payment of Performance Liquidated Damages does not in any way relieve the Contractor from any of its obligations to complete the Works or from any of its warranties, obligations or liabilities under or in connection with this contract.

(b) Without prejudice to clause 3.12(a), the payment of Performance Liquidated Damages under this clause 3 is in addition to any liability of the Contractor for Delay Liquidated Damages.

3.13 Rights at law

If this clause 3 (or any part) is found for any reason to be void, invalid or otherwise inoperative so as to disentitle the Owner from claiming Performance Liquidated Damages, the Owner is entitled to claim against the Contractor for damages at law for the Contractor's failure to meet the Performance Guarantees. Such damages must not exceed the amounts specified in the schedule of damages at law.

3.14 No benefit

The Contractor is not entitled to the benefit of the exclusion of liability for consequential loss under this contract in any claim for damages at law by the Owner against the Contractor pursuant to clause 3.13.

3.15 Duplicate damages

Nothing in this clause 3 entitles the Owner to claim duplicate damages at law or under this contract in respect of the failure of the Contractor to meet the Performance Guarantees, the Minimum Performance Guarantees or the Availability Guarantee.

4. Definitions

Availability Guarantee means the guarantee specified as the 'Availability Guarantee' in the [schedule of performance guarantees].

Availability Test means the test described as the availability test in the [schedule of tests].

Certificate of Commercial Operation means the certificate issued by the Owner under clause 2.2 in the form set out in the [schedule of forms of certificates].

Certificate of Final Commercial Operation means the certificate issued by the Owner under clause 2.4 in the form set out in the [schedule of forms of certificates].

Certificate of Final Completion means the certificate issued by the Owner under clause 2.5 in the form set out in the [schedule of forms of certificates].

Certificate of Mechanical Completion means the certificate issued under clause 1.1(b) in the form set out in the [schedule of forms of certificates].

Commercial Operation means the stage of the Works when the following has occurred:

(a) the Contractor has provided copies of the draft operation and maintenance manual

(b) the Emissions Guarantee Test has been passed

(c) the Noise Guarantee has been met

(d) one of the following has occurred:

  (i) the Performance Guarantees have been met

  (ii) the Minimum Performance Guarantees have been met and the Contractor has paid the applicable Performance Liquidated Damages

  (iii) the Minimum Performance Guarantees have been met and the Contractor has elected under clause 2.2(a)(iii) to exercise its rights under clause 2.3

(e) the facility is capable of being operated reliably, safely and efficiently under all anticipated or likely operational conditions

(f) the Contractor has provided the Spare Parts required to be provided by the Date for Commercial Operation

(g) the facility is in a condition which allows the Owner to comply with all laws relating to its operation

(h) all documents and other information in respect of the facility required under this contract have been supplied to the Owner or the Owner's representative

(i) all government approvals to be obtained by the Contractor under this contract and which are necessary for the operation of the facility, and to the full extent permitted by law, have been transferred (to the extent necessary and/or permitted at law) to the Owner or the Owner's nominee

(j) the facility is complete in all respects other than minor items that in the reasonable opinion of the Owner's representative will not prejudice (either by not being completed or as a result of the work needed to complete them), the ability of the Owner to operate the facility legally, safely, reliably and efficiently.

Commissioning means the operation of the facility, or any part, by the Contractor following Precommissioning in accordance with the [schedule of technical specification], which operation is to be carried out by the Contractor as provided in clause 1.3, for the purpose of preparing the facility for operation and the carrying out of the Performance Tests.

Commissioning Tests means the tests specified as commissioning tests in the schedule of tests.

Date for Commercial Operation means, in respect of the facility, the date specified in the [schedule of guaranteed dates], as may be varied in accordance with this contract.

Date of Commercial Operation means the date specified in the Certificate of Commercial Operation.

Defects Liability Period means the period of 12 months from:

(a) in relation to the facility as a whole, the Date of Commercial Operation

(b) in relation only to where a part or parts of the facility are repaired, replaced or made good, the date of commencement in accordance with the contract.

as the case may be.

Delay Liquidated Damages means the liquidated damages for delay specified in the [schedule of delay liquidated damages].

Emissions Guarantee means the guarantee specified in the [schedule of performance guarantees], which is an absolute guarantee and the meeting of which is a condition precedent to achieving Commercial Operation.

Emissions Guarantee Tests means the tests specified as the emissions guarantee tests in the [schedule of tests].

Environmental Guarantees means the Emissions Guarantee and the Noise Guarantee as specified in the [schedule of performance guarantees].

Final Commercial Operation means, where paragraph (d)(iii) of the definition of Commercial Operation applies, the stage of the Works when the following has occurred:

(a) Commercial Operation has been achieved

(b) one of the following has occurred:

  (i) the Performance Guarantees have been met

  (ii) if applicable, the Contractor has paid Performance Liquidated Damages in accordance with clause 3.5

(c) all other preconditions to Commercial Operation have been achieved, met or passed during the Subsequent Testing Period.

Final Completion means the stage of the Works when:

(a) Commercial Operation has been achieved

(b) if applicable, Final Commercial Operation has been achieved

(c) all defects and/or deficiencies have been satisfactorily remedied

(d) the Defects Liability Period has expired.

Mechanical Completion means that the facility has been completed mechanically and structurally in accordance with the [schedule of project technical requirements] and the other requirements of the contract such that in the reasonable opinion of the Owner's representative the facility is substantially completed and able to operate safely, reliably and efficiently and the facility is ready for Precommissioning and Commissioning.

Minimum Net Electrical Output Performance Guarantee means the minimum net output performance level specified in the [schedule of performance guarantees].

Minimum Net Heat Rate Performance Guarantee means the minimum net heat rate performance level specified in the [schedule of performance guarantees].

Minimum Performance Guarantees means the Minimum Net Heat Rate Performance Guarantee and the Minimum Net Electrical Output Performance Guarantee.

Noise Guarantee means the guarantee specified as the 'Noise Guarantee' in the [schedule of performance guarantees], which is an absolute guarantee and the meeting of which is a condition precedent to achieving Commercial Operation and Final Commercial Operation.

Overall Performance Test means a test in which the Performance Guarantees and the Environmental Guarantees are measured together.

Performance Guarantees means the performance guarantees to be met in relation to Commercial Operation and Final Commercial Operation as set out in the [schedule of performance guarantees] but does not include the Environmental Guarantees or the Availability Guarantee.

Performance Liquidated Damages means the liquidated damages for underperformance of the facility as specified in the schedule of performance liquidated damages.

Performance Tests means the tests specified as Performance Tests in the [schedule of tests].

Precommissioning means the testing, checking and other works specified in the schedule of technical specification to be performed by the Contractor in preparation for Commissioning.

Project means the development, design, financing, construction, commissioning, testing, delivery, operation and maintenance of the facility.

Service means the facility is available and is capable of meeting the Minimum Performance Guarantees, provided however that it is not in Service from the time ramp-down commences pursuant to a request from the Contractor under clause 2.4. If the facility is not generating electricity then the facility is not in Service from the time agreed between the parties following a request by the Contractor that it be taken out of Service pursuant to clause 2.3. If the parties cannot agree on the time then, provided that the Contractor has made a request pursuant to clause 2.3, the facility will be deemed to be out of Service for the time that the facility is not available.

Spare Parts means the spare parts the Contractor is obliged to provide pursuant to the contract that must, as a minimum, comprise the parts listed in the [schedule of project technical requirements].

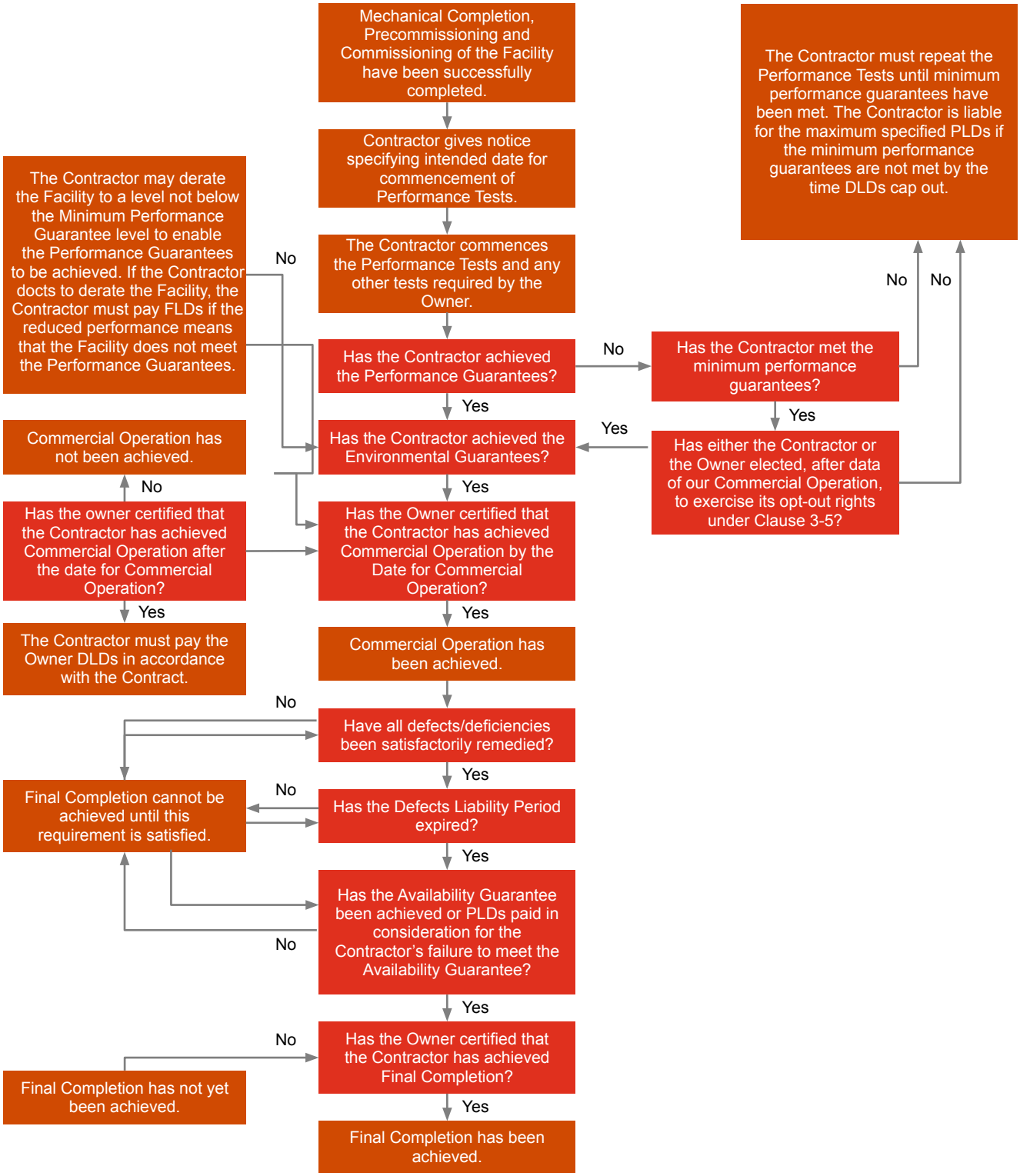
Subsequent Testing Period means the 60-day period after the Date of Commercial Operation as described in clause 2.3.

Works means all the equipment to be supplied and the whole of the work and services to be performed by the Contractor under this contract and as further described in the [schedule of technical specification] and includes any variation.



Appendix 3
Simple regime flowchart

Commercial operation, final completion and performance guarantees

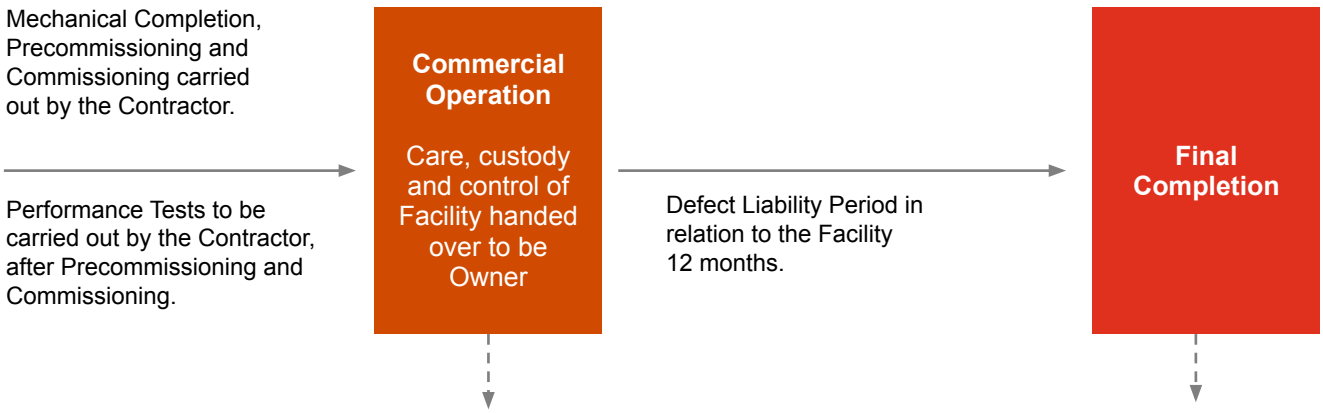


Appendix 4
Simple regime timeline

Simple regime completion

Notes on structure

The advantage of this regime is that the Owner does not assume care, custody and control of the plant (and thus does not assume responsibility or liability for it) until the Contractor has either met the Performance Guarantees or paid the appropriate Performance Liquidation Damages for its failure to meet the Performance Guarantees. This structure is more suitable where it is not viable to grant the Contractor any time after Commercial Operation in which to try and increase the Facility's performance.



Notes on Commercial Operation

In order to achieve Commercial Operation, the Contractor must fulfil the requirements set out in the definition of Commercial Operation, unless the Owner, in its absolute, sole and unfettered discretion, issues a Certificate of Commercial Operation, notwithstanding that all requirements have not been satisfied.

The Contractor may achieve Commercial Operation and be under no further obligation if the Performance Tests demonstrate that the minimum performance guarantees and the Performance Guarantees have been achieved, and all other preconditions have been met.

If either the Performance Guarantees have not been achieved but the minimum performance guarantees have, or both the Performance Guarantees and the minimum performance guarantees have not been achieved, the Contractor is obliged by Clause 3.2 to attempt to improve the performance of the Facility. Where this deferral means that Commercial Operation is not achieved by the Date for Commercial Operation, Delay Liquidated Damages will accrue; and the period in which this deferral and improvement will take place must end when the aggregate liability cap on Delay Liquidation Damages is reached.

Despite the fact that Clause 3.2 requires the Contractor to continue to improve the plant after the Date for Commercial Operation, provided that the minimum performance guarantees and the Environmental Guarantees have been met, at any time after the Date for Commercial Operation either the Contractor or the Owner may exercise their opt-out rights under Clause 3.5. meaning that further modifications will be halted and the Contractor's PLDs for any continuing failure to meet the Performance Guarantees will crystallise.

The Contractors is liable to pay Delay Liquidated Damages in any instance where it falls to achieve Commercial Operation by the Date for Commercial Operation.

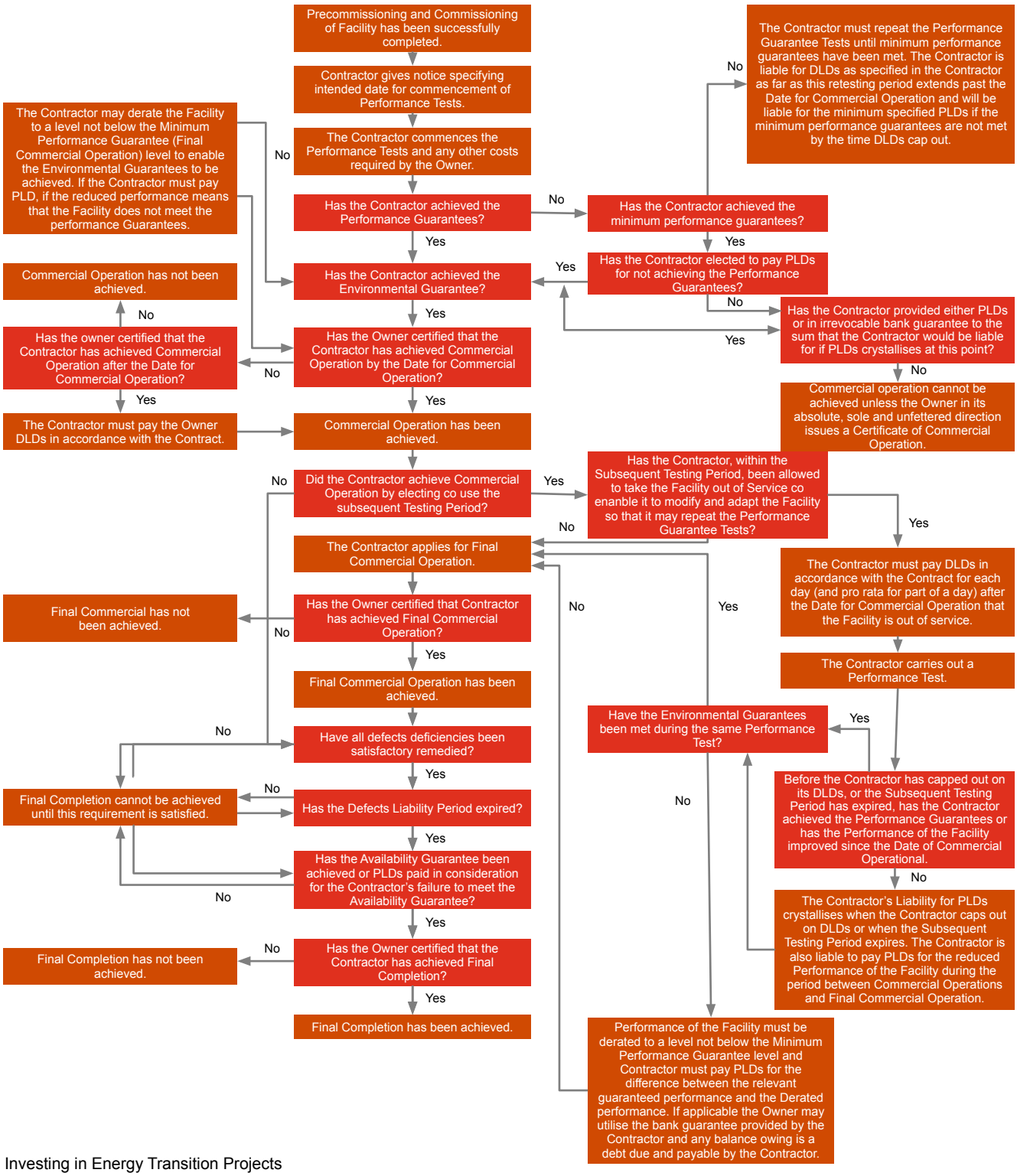
Notes on Final Completion

In order to achieve Final Completion, the requirements set out in the definition of Final Completion must be satisfied. If the Contractor has failed to achieve the Guaranteed. Availability set out in clause 3.8 following the Date of Commercial Operation, the Contractor must pay Performance Liquidation Damages.

Appendix 5

Detailed regime flowchart

Commercial operation, final commercial operation, final completion and performance guarantees

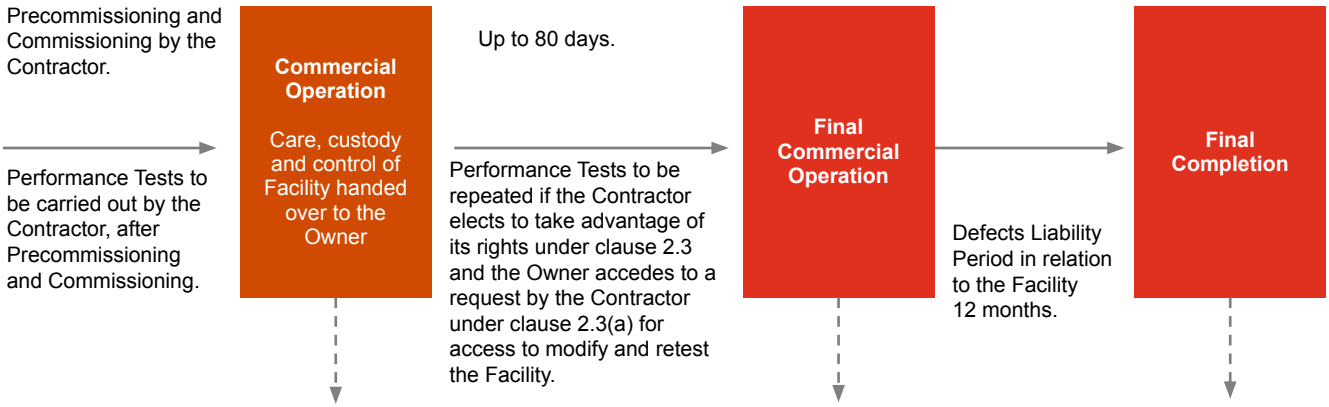


Appendix 6
Detailed regime timeline

Completion timeline

Notes on structure

The benefit of this process is that the Owner will be able to take possession of the Facility and begin generating electricity as soon as Commercial Operation is achieved (effectively, as soon as the minimum performance guarantees are met). This structure is most useful where it is viable to grant (in the Owner's discretion) the Contractor a Subsequent Testing Period in which to try and increase the Facility's performance, secured by advantage payment (or a guarantee) equivalent to the PLDs that would otherwise be payable.



Notes on Commercial Operation

In order to achieve Commercial Operation the Contractor must satisfy one of the three paragraphs in clause 2.2(a) unless the Owner, in its absolute, sole and unfettered discretion, issues a Certificate of Commercial Operation, notwithstanding that all requirements have not been satisfied.

The Contractor may achieve Commercial Operation and be under no further obligation if the Performance Guarantees have been achieved at the Performance Tests, and all other preconditions have been met.

If the Performance Guarantees have not been achieved but the minimum performance guarantees have, the Contractor may elect to exercise its rights under clause 2.3 and undertake further modifications during the Subsequent Testing Period. These rights are conditional on the payment of Performance Liquidated Damages or the granting of security, and may not be exercised once the Delay Liquidated Damages cap is reached.

If the Performance Guarantees have not been achieved but the minimum performance guarantees have, and the Contractor does not elect to take advantage of its rights under clause 2.3, it may pay Performance Liquidated Damages for its failure to achieve the Performance Guarantees and be released from further obligation.

The Contractor is liable to pay Delay Liquidated Damages for failure to achieve Commercial Operation by the Date for Commercial Operation.

The meeting of the Environmental Guarantees (Noise and Emissions is an absolute requirements to achieving Commercial Operation).

Notes on Final Commercial Operation

In order to achieve Final Commercial Operation the requirements set out in the definition of Final Commercial Operation must be satisfied. If the Contractor has failed to meet one or more of the Performance Guarantees, the Contractor must pay Performance Liquidated Damages in satisfaction of the relevant Performance Guarantees.

The Contractor is liable to pay Delay Liquidated Damages for each day after the Date for Commercial Operation that the Facility or part of the Facility is not in Service as a result of the Contractor electing to take advantage of its right under clause 2.3.

The meeting of the Environmental Guarantees is an absolute requirement to achieving Final Commercial Operation.

Notes on Final Completion

In order to achieve Final Commercial Operation, the requirements set out in the definition of Final Completion must be satisfied. If the Contractor has failed to achieve the Availability Guarantee over the 12 months following the Date of Commercial Operation, the Contractor must pay Performance Liquidated Damages.

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