FORCED MARRIAGES ON CONSTRUCTION PROJECTS:

THE GOOD, THE BAD AND THE UGLY

By Justin Mort QC

This paper was prepared by Justin Mort QC in advance of a panel discussion at the IBA in Korea of the same title. It is concerned with "marriages" forced on construction projects: where a specific subcontractor, consultant or supplier is imposed upon a contractor by the employer. In particular, this paper is concerned with the divorce stage: the relationship has failed and the parties are in formal dispute. Are there any particular challenges or hazards arising out of such a relationship?

Introduction

In the interests of simplicity the parties are referred to respectively as *"the employer"* (the party imposing the relationship on to its main contractor), *"the contractor"* (i.e. the main contractor: the party forced to enter into the relationship) and *"the subcontractor"*. The underlying assumption when using this terminology is that the employer/project owner has engaged a main contractor and has in some way compelled the contractor in turn to engage with a specific subcontractor (or as it may be a designer or other consultant or supplier or manufacturer).

The party being imposed upon the contractor may be a nominated subcontractor, whether in the formal sense of that phrase (e.g. as it is used in FIDIC contracts) or something less than that. It might be simply a named subcontractor or there might be a limited list of acceptable subcontractors, with the contractor permitted to choose the specific entity. This paper also anticipates a designer or other consultant imposed upon the contractor. A yet further scenario is where the employer imposes not an entity as such but a specified proprietary system or product (for example: a proprietary paint system, or a specific item of plant made by a named manufacturer) which in practice requires the contractor to contract either directly with the named manufacturer or with the manufacturer's sole authorised representative.

In practice there are also many cases where the main contractor imposes an arrangement on its subcontractor requiring the subcontractor to engage with some subordinate subsubcontractor or supplier. By using the terms as defined above (employer, contractor, subcontractor) it is not intended to exclude consideration of such cases (i.e. contractor, subcontractor, subsubcontractor) and the terms should be understood accordingly.

A defining characteristic of the *"forced marriage"* (as referred to in the title) is that the contractor is denied the freedom to choose its subcontractor, consultant or supplier. If the marriage is *"forced"* it must follow that, all things being equal, the nominated or named subcontractor or supplier would not have been the contractor's first choice.

The fact that the contractor is obliged to engage with a particular party that, but for that obligation, it would not otherwise have done may give rise to problems, that is to say: problems related to the party itself (e,g, as to its performance, or its solvency).

But the nature of the relationship (one imposed upon the contractor) may also have implications for the terms upon which these marriage-partners deal. In particular: the nominated or named subcontractor may have a particularly strong bargaining position if the contractor has been denied the freedom to engage an alternative. It may be able to name its terms generally, or to impose exclusions of responsibility or liability. Particular difficulties may arise in the case where the named subcontractor is imposed upon the contractor during the project i.e. post-contract, by way of a variation.

A further defining characteristic of the forced marriage, or rather the same point expressed slightly differently, is that the employer necessarily involves itself in a subordinate contractual layer, whilst (in theory at least) seeking to make an intermediate party (the contractor) contractually responsible for performance. That may mean, but does not necessarily require, a direct relationship of some sort as between employer and subcontractor. That may have implications for the contractor as discussed below, for example if the employer's long-term relationship with the subcontractor is more important to the employer than its relationship with the contractor. Of course, some main contractor provisions make specific allowances for the fact that the employer has restricted the contractor's choices in this way.

Forced marriages for the good and for other reasons

The reference in the title of this paper to *"the Good, the Bad and the Ugly"* alludes to the fact that there are a range of possible scenarios or types of scenario where a subcontract, consultant or supplier is imposed upon a contractor, and that some types of scenario may work out better than others. Similarly, the employer's motivation for imposing a particular subcontractor or consultant upon a contractor may vary.

Whilst it is not strictly necessary to allocate particular types of project scenario to any of the three characters in Sergio Leone's film of that title, nonetheless one can readily think of three contrasting *"forced marriage"* situations for the purposes of discussion.

The good

In this first category the employer wants nothing but the best for its project. It therefore imposes its choice of high-quality products or a reputable subcontractor(s) on the contractor for the critical elements of the project.

For example: the employer requires high quality manufactured by an internationally recognised company to be incorporated into its facility. In such a case it may be that:

(1) the plant or other product is known to be reliable and/or known to meet the employer's performance requirements;

(2) the employer has a successful past history of using this manufacturer or subcontractor and/or enjoys a good relationship with it as a result (and enjoys corresponding leverage on price);

(3) the employer invariably uses this product or system on all of its projects and wants consistency;

(4) the manufacturer or subcontractor provides effective and reliable post-project customer support;

(5) the subcontractor's size and financial standing is such that the end customer (in this case the employer) can confidently rely upon collateral warranties in the event of any problems.

The contractor is therefore obliged to engage (in this example) that named manufacturer, subcontractor or supplier. The marriage is *"forced"* in the sense that but for the employer's requirements the contractor would or might have used a less reputable but cheaper alternative.

In those circumstances the downside for the contractor is that it may be denied the opportunity to make as much profit as it would have done had it been permitted to choose its own supplier simply on grounds of price.

On the positive side the contractor is effectively compelled to provide a quality project and one that corresponds with what the employer wants, and on the basis that the employer is by implication content to pay for this high standard. In addition: in this scenario the employer is more likely to have effective remedies directly against the nominated or named supplier in the event of defects or non-performance. Indeed, the possibility of an effective direct remedy against the nominated subcontractor may have been a consideration in the employer's original decision making. In theory that might reduce the employer's need to pursue the contractor in relation to the same matters.

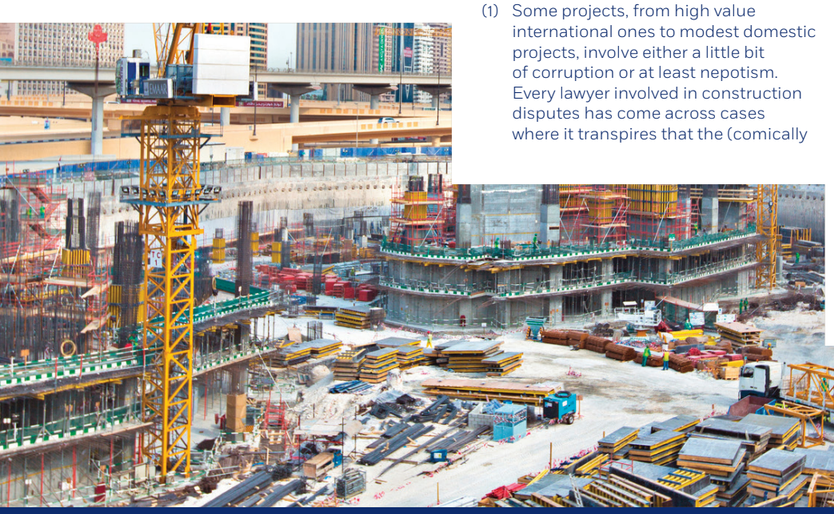
These points are likely to be in the contractor's interest.

A similar scenario is where the employer requires the contractor to engage a well-recognised engineering practice or other design consultant, again with an eye to either (1) ensuring a project of good quality, and/or (2) procuring effective and enforceable warranties to be provided by the consultant (albeit a consultant engaged by the contractor) directly to the employer for the purposes of any issues that might arise after completion of the project.

The bad

At the opposite extreme the marriage is imposed upon the contractor for reasons that have nothing to do with ensuring a high-quality project but for other considerations.

The most obvious reason might be that the employer is concerned to keep costs down. It has identified a subcontractor, manufacturer or supplier who the employer believes meets its requirements (just about) but more importantly fits the budget.



But there are myriad other reasons why the employer might require the contractor to engage with identified or nominated subcontractors who fall short in terms of quality.

A recurring theme of many international projects is a requirement to engage labour and/or businesses local to the project site. From a moral, economic and/or commercial perspective it is entirely right that a significant enterprise (such as an engineering project or the construction of a manufacturing facility) will benefit the local economy and the individuals living in the surrounding environment and affected by it. No one could seriously suggest otherwise.

Conversely the idea that global businesses should make vast profits from the natural resources of say a developing country whilst effectively preventing the region from sharing in the benefit is surely abhorrent to anyone with any sense of fairness.

One way for the employer to satisfy that moral imperative at little personal cost is to require the contractor to engage subcontractors local to the project. The employer can thereby advertise its commitment to the use of local businesses for its lucrative projects (what might be referred to as virtue signalling). The actual interface with the local businesses, and any problems arising (for example: because the local subcontractor has no experience of this kind of project), are the responsibility of the contractor and the contractor's problem.

In addition to this slightly cynical scenario there may be other practical and/or legislative requirements that compel the engagement of either a specified local subcontractor, or local subcontractors or labour generally.

By way of example:

(1) Some projects, from high value international ones to modest domestic projects, involve either a little bit of corruption or at least nepotism. Every lawyer involved in construction disputes has come across cases where it transpires that the (comically unsuited) subcontractor imposed upon the contractor by the employer is owned by a connection of the employer.

(2) Local legislation (for example: legislation governing the licencing and/or authorisation of contractors or legislation governing health and safety matters) may mean that the contractor has to engage a local subcontractor, or simply require that a minimum number of local people are employed on the project. In remote regions and/or in the case of highly specialist trades that may mean that the contractor has an effective choice of only one or two subcontractors.

(3) The authority responsible for permitting the works may require the engagement of local subcontractors for specified tasks and/or local labour as a condition of the works proceeding.

In all of these situations, in contrast to the first category, the common theme is that the subcontractor imposed upon the contractor has not been selected because of its established credentials but for some reason unrelated to the quality or anticipated quality of its output. In such scenarios, because of its position in the contractual chain (that is to say: in the middle), the contractor is then expected to make good any shortfall in quality.

The ugly, aka: the "design and dump"

Since there are three main characters referred to in the title of the film there needs to a third scenario (*il brutto*). This would be the *"design and dump"* form of contract.

> *"The intention behind the "design and dump", that is to say: the employer's intention, is that if there is anything wrong with or difficult/impossible about the design such matters will be the contractor's responsibility and liability."*

In this type of scenario the employer puts together its chosen team of designers, some high level or outline drawings and some similarly high level performance based specifications. Everything is driven entirely by price.

The employer then engages the contractor on a design and build basis, requiring it to take over the entirety of the design team (pursuant to a complicated novation arrangement or some equivalent process), together with such design as has been prepared to date by the design team for the employer. Thereafter the contractor is required to develop the rudimentary outline specification into a detailed design and then to proceed to build out the project.

One sometimes encounters this strategy in the context of disputes arising out of hotel, residential or other building projects in the UK and the Middle East. The developer employer wants to build say a hotel of five-star quality but expending only the cost of a budget hotel. The design and dump contractor has been brought in to the project in order to solve this arithmetical conundrum.

The intention behind the *"design and dump"*, that is to say: the employer's intention, is that if there is anything wrong with or difficult/impossible about the design such matters will be the contractor's responsibility and liability.

Invariably the different elements of the design, being only preliminary at contract stage, will have not been co-ordinated with one another at the time that the design and dump contract is signed. The sort of problem that seems to arise in every such case is that (for example) there is a hopelessly inadequate amount of space allowed in the architect's preliminary layout drawings of the building(s) available to accommodate the ambitious quantity of lifts, plant and other services referred to in the M&E consultant's specification.

As indicated under the design and dump contract the idea is that upon contract execution all such problems (together with the entire design team responsible) are passed over to the contractor's side of the bargain. Whether in practice the terms of the contract do achieve that outcome (i.e. whether the contract terms successfully render the contractor liable for problems in the employer's design prepared before the contractor was engaged) may be a different matter.

In practice the contractor is unlikely to have had more than a limited opportunity to review, analyse and assess the employer's design at the time of tendering for or entering into the contract. Apart from any other consideration the contractor is unlikely to have retained its own full complement of engineers, architects, building services engineers etc in circumstances where the intention is that the contractor will take over and pay for the employer's entire team.

As a result at bid stage the design and dump contractor has to rely somewhat blindly upon the employer's design team having done a competent job to date, i.e. competent having regard to what the contractor now has to do (as opposed to: competent for the employer's rather more limited purpose, which was to hook and reel in the design and dump contractor).

In the event of the inevitable disaster in theory the contractor then has a complicated claim against the relevant consultant(s). That is to say: a claim in relation to services provided to a different client (i.e. the employer), for a different purpose, at a time when the contractor was not a participant in the project (i.e. pre-contract) and therefore in circumstances and/or upon the basis of instructions about which the contractor may know comparatively little.

In the design and dump the *"marriage"* or marriages are *"forced"* in that the contractor will necessarily have had no input into selection of the design team upon whom it is now wholly dependent: the bride and groom(s) will have never met before.

But not only that: crucially the contractor takes on not just someone else's design team but (depending upon the effectiveness of the *"dump"* provisions in the contract) also a large amount of design work carried out before it had any involvement.

To be clear: there is no standard form of design and dump contract. The employer typically uses either its own tried and tested form for this method of procurement or more likely a magnificently amended standard form of design and build contract. Extensive amendments to the standard form are necessary in this context because published forms of design and build contract do not ordinarily purport to make the contractor liable for inadequacies in design work carried out long before it had anything to do with the project.

The divorce, and problems at the dispute stage

Having identified some different *"forced marriage"* scenarios the purpose of this paper is to consider what if any issues might arise at the disputes stage.

There are a number of potential risks faced by any main contractor, sitting in the middle of a contractual chain i.e. irrespective of any element of *"forced marriage"*. For example:

(1) a failure and/or an inability at the procurement stage to align the subcontractor's or supplier's obligations and liabilities with the contractor's responsibilities to its customer;

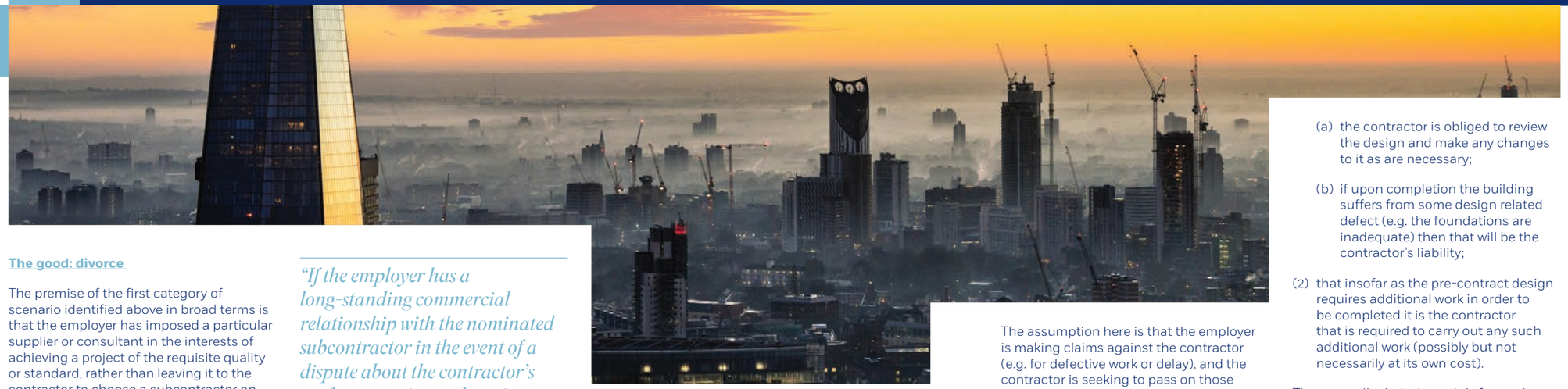
(2) the risk that formal proceedings upstream and downstream are required to be conducted

  (a) in different forums (e.g. court and arbitration)

  (b) before different tribunals

with a consequent risk of inconsistent findings (so that for example the contractor is found to be liable to the employer for say defective work but fails to establish the same defects as against the subcontractor).

To what extent, if at all, are those risks any different in the case of the forced marriage and/or in the different categories of forced marriage identified above?



The good: divorce

The premise of the first category of scenario identified above in broad terms is that the employer has imposed a particular supplier or consultant in the interests of achieving a project of the requisite quality or standard, rather than leaving it to the contractor to choose a subcontractor on the basis of cost and/or how much profit it can make from the project.

In that relatively happy scenario many such risks may well be significantly reduced. The employer's requirement for quality itself means that it is more likely to be content with the project outcome.

Moreover: the likelihood in this scenario is that the main contract specification will have been drawn up by the employer either with extensive input from the named supplier or subcontractor or at the very least with their proposed products or outputs specifically in mind. In those circumstances the possibility that there is some unfortunate disconnect as between the employer's requirements imposed upon the contractor and the terms of the relevant subcontract ought to be reduced. At the very least the employer can have less scope for complaint about (its) choice of product. Under English law at least, absent effective express terms to the contrary, the employer would struggle to bring a claim for fitness for purpose in relation to a product or system that it had itself chosen (*IBA v EMI & BICC Construction*[1]). It may nonetheless be entitled to bring a claim in relation to quality i.e. notwithstanding the fact that the product complained of was chosen by the employer.

Having said all of that there may be additional problems specific to this type of scenario in the event of a major dispute.

Firstly: this *"good"* scenario is assumed to arise out of the employer's devotion to the nominated or named subcontractor, its products or outputs. That is likely to have given the nominated subcontractor a particular advantage at the negotiating stage. In terms of price: since any price is likely to be passed on to the employer in theory that should not give rise to any issue for the employer. The issues are more likely to relate to the terms upon which the nominated subcontractor was engaged, which may be more difficult to pass up to the employer.

"If the employer has a long-standing commercial relationship with the nominated subcontractor in the event of a dispute about the contractor's performance it may have interest in seeking to maintain and/or further that relationship at the contractor's expense."

Crucially subcontractors in a strong negotiating position of that sort are typically inclined to limit or exclude their liabilities in the event of delay or defective work on their part. In addition, the subcontractor in a strong negotiating position may have been able to limit the standard of performance required so that, for example, it is obliged to exercise only reasonable skill and care in circumstances where the contractor is under a fitness for purpose warranty. Obviously these sorts of issues are likely to become relevant once the employer seeks to make claims against the contractor.

In addition, if the employer has a long-standing commercial relationship with the nominated subcontractor in the event of a dispute about the contractor's performance it may have interest in seeking to maintain and/or further that relationship at the contractor's expense.

Such a strategy could manifest itself in a number of ways:

(1) by the employer seeking to frame any claim against the contractor in a such a way as to make it difficult for the contractor to pass on those complaints to the subcontractor with the benefit of the special relationship with the employer;

(2) by the employer and the subcontractor sharing confidential information with one another relating to the contractor's disputes with each party.

The bad: divorce

However at least in the first type of scenario the subcontractor has been chosen because of its perceived competence, reputation or resources i.e. for reasons that are essentially good in terms of the likely success of the project. Different sorts of problem arise in the second scenario where the subcontractor has been imposed upon the contractor for reasons that have nothing to do with quality of work product and/or at the expense of quality.

If a subcontractor has been imposed simply on grounds of cost rather than quality or reliability that may give rise to problems.

But some specific problems may arise where the contractor has been compelled to engage with a local subcontractor:

(1) local standards to which the subcontractor is prepared to work may differ from or be irreconcilable with the international standards that the contractor has signed up to;

(2) the local subcontractor may only be prepared to work on the basis of a subcontract subject to local law (and expressed in the local language), and/or enforceable in the courts local to the project.

Businesses trading internationally are sometimes prejudiced against or at least nervous of the courts of other jurisdictions, and the fairness of a dispute resolution process where they are the foreigner and the other party is local. That is hardly surprising in the case where the relevant business in fact has limited or no experience of the local court, quite aside from difficulties arising from the enforcement of foreign court judgments as contrasted with arbitration awards.

But quite aside from such nervousness there are potentially severe practical disadvantages in conducting litigation under a foreign legal system and in a foreign language. The contractor will have to engage a local law firm (or a locally qualified branch of its regular lawyers, in any event: different people).

1 (1980) 14 BLR 1

The assumption here is that the employer is making claims against the contractor (e.g. for defective work or delay), and the contractor is seeking to pass on those claims to the subcontractor. There is obviously an immediate risk of inconsistent outcomes if the two sets of proceedings are to be conducted in different forums (i.e. the contractor found liable to the employer but unable to establish liability, in relation to precisely the same matters, as against the subcontractor). But that risk is likely to be magnified considerably in the case where the two sets of proceedings are to be determined by reference to different legal principles, contractual obligations expressed in different languages, and where the proceedings are to be conducted by different lawyers.

The ugly divorce

As for the design and dump contractor: it faces a number of possible disputes arising from the nature of its contract.

The issue that typically arises as between the contractor and the employer is whether the employer, by its contract terms, has successfully made the contractor responsible for any design issues created before the contractor had any involvement and which were therefore imposed upon it.

The employer's first difficulty is that its intention under the contract (to make the contractor responsible for past errors) is in a sense at odds with the factual history. Of course, in principle contracting parties are limited, in terms of what they may agree to be the position, only by their imagination. Nonetheless a contractual provision that purports to mean that a contractor is responsible (for all purposes) for a design that was self-evidently not the contractor's design but the employer's has to be robustly worded.

A related difficulty is that any reference to *"responsibility"* for design, or any equivalent phrase, is typically capable of a number of meanings. It can mean:

(1) that if the pre-contract design were negligently prepared and/or is not fit for purpose then the contractor is responsible; in practice that means that

   (a) the contractor is obliged to review the design and make any changes to it as are necessary;

   (b) if upon completion the building suffers from some design related defect (e.g. the foundations are inadequate) then that will be the contractor's liability;

(2) that insofar as the pre-contract design requires additional work in order to be completed it is the contractor that is required to carry out any such additional work (possibly but not necessarily at its own cost).

These are all relatively straightforward matters and in practice are unlikely to give rise to vast disputes.

But what the design and dump employer typically wants is that, in the event that the design cannot in fact be achieved (e.g. because it is literally physically impossible, for example: as per the example given earlier there is insufficient physical space for the specified services), the cost of any delay and/or additional building work arising out of a substantial re-design will be met by the contractor.

In practice that can be a difficult obligation to impose upon a contractor. The underlying presumption, absent some clear words to the contrary, is likely to be that the contractor is not responsible for additional costs arising from the fact that a design prepared by the employer is literally impossible. In practice it is relatively rare to see a contract that says in terms that not only are deficiencies in the employer's design to be addressed by the contractor but that additional cost arising from the corrections of such deficiencies (in terms of additional construction work) will be entirely borne by the contractor.

There is nonetheless plenty of scope for the contractor to face claims from the employer, as the full horror of its obligations become manifest during the course of the project. That then raises the possibility of the contractor seeking to pass on such claims to the novated design team, i.e. a group of consultants working for the employer at the time that the alleged crimes were committed. In addition, contractors sometimes have claims where either (1) the project has been over-designed, so that the quantity of structural work imposed by the design is unnecessarily great, or (2) under-designed, with the result that the contractor has bid too low.

Such claims have all the problems of any professional negligence claim of that type, i.e. ignoring for the moment the "forced marriage" element:

(1) there are bound to be difficult issues of causation and quantum where the complaint is that the contractor's tender sum was in the wrong amount;

(2) net contribution clauses are commonplace, and in any case where there are other potential candidates for blame make proceedings pointless, particularly if any of the claims is required to be conducted in arbitration (i.e. in isolation).

But in addition, claims by a design and build contractor against a member or members of the novated design team (i.e. a team originally engaged by the employer but transferred to the contractor) are particularly perilous for the reasons intimated earlier in this paper.

It is assumed for present purposes that the relevant design work of which complaint is now made will have been prepared not for the contractor (i.e. post-contract) but for the benefit of the employer, for the purposes of letting the project. The notorious Scottish case of *Blythe & Blythe v Carillion*[2], whether or not correctly decided, illustrates the sorts of problems that can arise where a contractor seeks to pursue a consultant that has been foisted upon it in relation to services provided to the original client (the employer).

Conclusions

Since the title of the paper assumes a range of different scenarios to some extent it is difficult to identify common themes.

But a common feature or by-product of any imposed marriage is likely to be the partial or wholesale imposition of subcontractor terms that the main contractor will have some difficulty rejecting, in circumstances where it is denied freedom to contract with whom it chooses. In practice that is likely to have a range of different implications for the contractor, from how disputes are to be resolved to the exclusion of liabilities by the subcontractor or other commercial matters.

A further common feature of any imposed marriage is likely to be a lack of familiarity or prior relationship between the main contractor and the imposed marriage-partner. In general construction projects will be successful because of good commercial and/or cultural relationships and attitudes between the project participants, more than anything that the lawyers contribute, or so one assumes.

2 (2001) 79 Con LR 142