

## **Alliancing in Australia under NEC**

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Alliance contracting is staging something of a comeback in Australia, because Australian governments and other project owners are increasingly seeing alliance contracting (and other forms of collaborative contracting) as an effective way to achieve value for money in Australia's overheated civil engineering and construction market.

At the same time, momentum is building within Australia's construction industry for governments and other project owners to make greater use of the NEC contract suite because it is seen to encourage greater collaboration than the forms of construction contract commonly used in Australia.

Alliance contracting continues to set the high-water mark for collaborative contracting. So those project owners that really want to embrace collaborative contracting should consider NEC's standard form alliance contract (ALC4).

But Australia has more experience with alliance contracting than any other country, and has grown familiar with alternative forms of alliance contract. It therefore remains to be seen whether Australian project owners' will embrace ALC4 over the forms of alliance contract presently used in Australia. This article identifies the key differences between ALC4 and Australian alliance contracts that Australian industry participants will wish to consider.

### **How does ALC4 compare with Australian alliance contracts?**

Australia doesn't presently have a standard form alliance contract. But it came close with the template Project Alliance Agreement published by the Federal Department of Infrastructure and Regional Development in 2015. Other forms of alliance contract that the Australian market is familiar with include:

- the model Project Alliance Agreement once published by the now defunct Alliancing Association of Australasia, and
- the forms of Project Alliance Agreement used by various state government agencies such as Roads and Maritime Services, Transport for NSW, VicRoads, Level Crossing Removal Authority, Rail Projects Victoria and Sydney Water - each of which are slightly different, and have evolved over time.

ALC4 embraces most of the key concepts found in these Australian forms of alliance contract. However, there are several differences which make ALC4 less "owner-friendly" than Australian alliance contracts.

### **An integrated team, and consensus based decision making for all decisions**

Like Australian alliances, ALC4 contemplates the establishment of a single integrated project team comprising individuals from the owner and each non-owner participant.

Each member of the alliance is represented on the Alliance Board, which sets the strategy for achieving the objectives of the alliance, agrees the allocation of work within the alliance, and makes strategic decisions.

There is no superintendent, client's representative or project manager, as found in more traditional construction contracts including NEC's Engineering and Construction Contract. Rather, the Alliance Board appoints an Alliance Manager, to manage the work on behalf of the Alliance Board. The individual appointed to this role could be employed by the owner, or by a non-owner participant.

Decisions of the Alliance Board require unanimous agreement, so each member of the Alliance Board effectively has a right of veto. There is no concept of decisions that are reserved for the owner alone, as found in many Australian alliances.

Decisions which the Alliance Board is unable to achieve consensus can be referred to an independent expert for a non-binding opinion to be used by the Alliance Board to assist it in finally resolving the matter, but there is no deadlock breaking mechanism. This approach - which effectively forces the parties to achieve consensus in order to move forward - is consistent with the 'pure' alliance approach found in the model Project Alliance Agreement previously published by the Alliancing Association of Australasia. But the absence of a deadlock breaking mechanism exposes the parties to the risk that part or all of the contract could become a legally unenforceable 'agreement to agree', which is why most modern Australian alliance contracts include a deadlock breaking mechanism.

### **No blame**

A fundamental feature of the 'pure' alliancing model that evolved in Australia was the concept of no blame. Each participant in the alliance, including the owner, agrees to release all other participants from legal claims arising from their participation in the alliance, except in the case of a wilful default.

ALC4 embraces this concept by treating all uninsured liabilities incurred by a participant as an alliance cost (except for liabilities to third parties arising from an intentional act or omission in breach of the contract, which are to be borne by the defaulting participant). However, ALC4 departs from the Australian approach by:

- allowing the owner or another participant to bring a claim against a participant for negligence;
- making the resultant liability, to the extent it is not insured, an alliance cost that must be reimbursed by the owner; and
- sharing the 'pain' of this additional alliance cost between all participants in accordance with the agreed gain/pain share regime.

An advantage of this approach is it overcomes the need for a bespoke professional indemnity insurance policy - to respond to a claim by the owner or a non-owner participant arising from the professional negligence of another participant despite the participant having no liability upon such a claim by virtue of the broader 'no blame' clause found in Australian alliance contracts.

## **Remuneration including gain/pain share**

ALC4 adopts the 3-limb Australian alliance remuneration model in that:

- all direct costs incurred by the non-owner participants are reimbursed by the owner, even if they exceed the budget;
- each non-owner participants receives a fee on account of profit and contribution to its corporate overheads; and
- the non-owner participants receive a gain-share payment from the owner if an aspect of the works achieves or exceeds the agreed target for an alliance objective, or pay a pain-share payment to the owner if an aspect of the works does not meet an agreed target.

However, it differs from the Australian model in that:

- the fee is not an agreed lump sum amount. Rather, it is calculated by applying each non-owner participant's stated "fee percentage" to the actual direct costs incurred by that participant;
- there is no mechanism for interim payments of gainshare or painshare, in advance of final completion;
- if the alliance costs are less than the budget/target cost, the cost savings are shared, even if other alliance objectives are not achieved. A common approach in Australia is to add the cost savings to the total gainshare amount available to the non-owner participants if they achieve other alliance objectives; and
- the liability of non-owner participants to share the pain of cost overruns is not necessarily capped at an amount equal to its fee, although there is the ability to achieve this result by utilising the optional limitation of liability clause.

The ALC4 approach to calculating the fee can create a perverse incentive, as an increase in the non-owner participant's direct costs results in an increase to its fee. Care needs to be taken to ensure that the painshare payment incurred by a non-owner participant due to a cost overrun arising from its inefficiency exceeds the resulting increase to its fee, to avoid perverse outcomes.

## **Scope variations and other adjustment events**

Australian alliance contracts only allow the budget and other targets/KPIs to be adjusted in very limited circumstances. In particular, variations to the scope of works do not result in an adjustment to the budget, target completion date or other targets/KPIs, unless all participants including the owner agree that the variation is a 'major variation'.

ALC4, on the other hand, treats every scope variation as a compensation event that entitles the non-owner participants to an adjustment to the budget, target completion date and/or other performance targets, even if it is a minor variation.

Like most Australian alliances, the adjustments to the budget, target completion date and/or other performance targets are to be unanimously agreed by the Alliance Board under ALC4.

Undoubtedly, the additional risk taken by non-owner participants under the Australian alliance model results in higher allowances for risk and, hence, a higher agreed budget. But the trade-off for owners is that the agreed budget under ALC4 is unlikely to prove to be as reliable an indicator of the actual outturn cost for the owner, as has been the case under Australian alliances.

### **Termination for convenience**

Australian alliance contracts generally give the owner the right to terminate the agreement for convenience, subject to the owner reimbursing the non-owner participants for all direct costs incurred prior to and as a consequence of the termination, together with a portion of the fee and gainshare/painshare payment based on the proportion of the works completed at the time of termination.

ALC4 adopts a different approach. It only allows the owner to terminate the alliance for convenience, if all other participants agree. This significantly limits the options available to the owner to manage the risk of a major cost overrun, especially if the pain-share liability of the non-owner participants is capped at the amount of their fee.

### **Fiduciary obligations and good faith**

Like all NEC contracts, ALC4 requires the parties to act in a spirit of mutual trust and cooperation. While the legal meaning of this obligation is somewhat uncertain, it is clear that it does not require a party to put the commercial interests of the other parties ahead of its own commercial interests.

However, it has long been acknowledged in Australia that the express commitments commonly included in alliance contracts - such as the commitment to make decisions on a "best for project basis" - may inadvertently give rise to a fiduciary relationship.

A fiduciary relationship arises when one person is able to take advantage of another, who places trust, reliance and confidence in him or her by reason of his or her experience, position or influence. If such relationship is held to exist, then the law will impose fiduciary obligations on the fiduciary. Examples of fiduciary relationship include partners in a partnership, trustee and beneficiary, agent and principal, ward and guardian, lawyer and client, and doctor and patient.

While a typical project alliance does not create legal partnership relationship, there is legal authority for the proposition that parties to a joint venture agreement can assume fiduciary obligations, depending on the terms of their agreement.

If an alliance results in a fiduciary relationship, the obligations of the alliance participants will be significantly more onerous. In particular, participants would be obliged to act with utmost good faith, and put the interests of the other participants ahead of their own. Participants would also be precluded from using knowledge or opportunities obtained as a result of their participation in the alliance for the advantage of themselves or a third party, or to the disadvantage of the other participants.

To avoid such outcomes, many Australian alliances expressly deal with this issue, for example, by making it clear that the owner can act in its own self-interest when exercising its reserved powers. Parties proposing to use ALC4 would be wise to get legal advice on this issue.

### **Optional clauses provide additional flexibility**

ALC4 can be used as a 'project alliance agreement' to cover a single project, like the Australian forms mentioned above. However, it has been drafted so that it can also be used as a 'program alliance agreement', covering a program or series of separate projects, by selecting the appropriate optional clause.

ALC4 also incorporates an optional clause that allows the contract to be used for a two stage alliance where the project delivery phase (stage two) only commences if the Alliance Board accepts a proposal at the conclusion of the project development phase (stage one) that details the impact of stage two on the scope, budget, target completion date and other performance targets. This avoids the need for a separate preliminary alliance contract, as sometimes occurs for Australian alliances.

Finally, ALC4 includes an optional clause dealing with BIM (building information modelling). This, coupled with the documentation of the necessary intellectual property rights between all alliance participants in a single agreement, and the liability and gain/pain sharing regime, makes it easier to successfully implement BIM.

### **Country specific clauses for Australia**

NEC is yet to publish any country specific clauses that should be added to its contracts when using them in Australia, so parties proposing to use ALC4 should seek appropriate legal advice. Many owners, particularly government agencies, will also want to add client specific provisions to ALC4 to cover government policies, proportionate liability, WHS (including appointment of a principal contractor), greenhouse gas and energy reporting requirements, personal property security issues and other statutory requirements - which often differ between Australian states and territories.

### **Conclusion**

ALC4 will almost certainly find a place in the Australian construction contracting scene, as it embraces most of the key concepts that that Australian industry looks for in its alliance contracts, and is shorter, simpler and easier to use than the forms of alliance contract presently used in Australia.

The differences from the forms of alliance contract seen to date in Australia will make it particularly appealing to non-owner participants, who are crying out for Australian governments to adopt a more sustainable approach to the procurement of construction services.

Project owners who are looking for a solid but simple form of alliance contract that can be used as part of a contracting suite that covers traditional fixed price procurement methods as well as more modern relational contracting approaches, will like ALC4 and its companion contracts within the NEC4 suite.

But we'll likely see some 'Z clauses' - NEC speak for additional clauses added by the parties to address client or project specific issues that are not otherwise addressed in the template, or to adjust the template's risk allocation - emerge from Australian project owners looking for greater control over their alliance projects. Z clauses should, however, be kept to a minimum to maintain the efficiency benefits that come from using a standard form with which market is familiar.

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