The Prevention Principle:

how it relates to liquidated damages
and the role of the superintendent

Hugh Davis | 20 April 2016
What I’m going to cover…

1. Briefly summarise the development of the law surrounding the prevention principle
2. Propose a formulation for the PP and consider the superintendent’s role in its application
3. Consider the current state of this area of the law in Australia
4. Review a recent adjudication where I considered a liquidated damages (LDs) claim levied by the main contractor against the subcontractor
What is the prevention principle?

Stems from the principle that a party cannot benefit from its own wrong…

A principal ‘cannot insist on a condition if it is his own fault that the condition has not been fulfilled’

*Amalgamated Building Contractors v Waltham Holy Cross UDC* [1952] 2 All ER 452, 455 (Denning LJ)
What is the prevention principle?

May be a ‘positive rule of law, not an implied term’

*SMK Cabinets v Hili Modern Electrics* [1984] VR 391, 394 (Brooking J)

In 11th ed of *Hudson’s Building and Engineering Contracts* (at 1155), **Ian Duncan Wallace** says this view is ‘persuasive’ and that, if the prevention principle were based upon an implied term, that term would be implied by law into construction contracts ‘and probably many other classes of contract generally.’ (unfortunately no detailed discussion on jurisprudential basis in 12th ed)

**BUT**, as Brooking J notes (at 395), ‘largely of academic interest’ because principle can be excluded / modified by contract
Brief History
How the prevention principle lurks in the background of construction contracting

Drafting of most standard-form EOT regimes is informed by the seminal English Court of Appeal case, *Peak v McKinney* (1970) 1 BLR 111.

**Facts:**
- Liverpool Corp (L) contracted Peak (P) to construct certain high-rise buildings
- P subcontracted McKinney (McK) to do foundations
- Some foundations were defective > substantial delay whilst:
  - P and L tried to work out what to do (52 weeks)
  - McK undertook rectification work (6 weeks)
- Under head contract, P was liable to L for 58 weeks’ LDs
- P sought payment from McK under terms of subcontract which was back-to-back with the head contract
- P did not grant McK an extension of time

*What happens next…?*
Peak had a very bad day at the Court of Appeal…

• Impossible to say (as referee had at first instance) that entirety of 58 week delay ‘flowed naturally and in the ordinary course of things’ (Hadley v Baxendale 1st limb) from McK’s breach (defective piling)

• Further, the Court was unable to apportion responsibility for delay because it could only apply the contractual machinery
  – i.e. unable to expunge the delay effect of P’s prevention to set new date for completion
Peak had a very bad day at the Court of Appeal…

• P could not unilaterally extend time if no contractual right to do so (as there was no provision in the subcontract)
• No date from which LDs could be calculated
  – time was ‘at large’ i.e. McK’s obligation became to complete within a ‘reasonable’ time
  – ‘if the failure to complete on time is due to the fault of both the employer and the contractor… the (LDs) clause does not bite’ (Salmon LJ at 121)
• At 121, Salmon LJ expressed the view that LDs clauses are for the benefit of the principal and as such were to be read strictly contra proferentem
And the upshot?

- P had **no** entitlement to LDs **at all**
- Any entitlement to **general law damages** limited by LDs which would have been payable
  - some doubt cast on this principle recently in academic writings but it is consistent with underlying principle that a party cannot profit from its own wrong
Formulation of the PP In light of *Peak* and *SMK Cabinets*...
The contractor’s primary obligation to the principal:

The contractor **must** achieve practical completion by the date **for** practical completion
For what events *must* an extension be granted?

In order to retain its entitlement to levy LDs if the contractor fails to achieve PC by the date for PC, the principal *must* grant an EOT for ‘acts of prevention’
The prevention principle may be formulated as follows...

• A principal will lose its entitlement to LDs if some of the delay is due to an act of prevention, unless:
  – There is a contractual mechanism to extend time for acts of prevention:
    1. where **claim by contractor**; and
    2. unilaterally, where **no claim** (or no valid claim) by contractor
      – Without this, the preventive effect is not expunged
      – Unilateral extension power acts as a safety release valve
  – It exercises its unilateral power and grants an extension of time for its acts of prevention
The prevention principle may be formulated as follows…

- This will be the case even if the principal’s delays form only part of the total delay.
- Even if the contractor would have been unable to complete on time in the absence of a delay by the principal, the LDs clause will still cease to apply if the principal is responsible for some of the delay.
- If the LDs clause is held inoperative because of the application of the PP, the principal will still be entitled to sue the contractor for any general law damages that it can prove flow from the contractor’s default.
Defining ‘act of prevention’

• An act of prevention is an act or omission by the principal that prevents the contractor from performing the contract according to its terms.

• In order to be effective, wording in contract needs to encompass *(SMK Cabinets, 395-6)*:
  – Acts
  – Defaults
  – Omissions
  – Variations

• This wording appears in most standard form construction contract EOT clauses.
The Superintendent
The role of the Superintendent

• The unilateral power to extend time is usually vested in the superintendent
• In *Perini v Commonwealth* [1969] 2 NSWR 530 at 536, Macfarlan J considered the inherent conflict of interest that can arise when a superintendent performs the dual role of agent and certifier
• His Honour found that, when acting as certifier, the superintendent is obliged “to act fairly and justly and with skill to both parties of the contract”, a term now implied at law into every construction contract unless expressly excluded
  – see *Kell & Rigby Holdings Pty Ltd v Lindsay Bennnelong Developments Pty Ltd* [2010] NSWSC 777)
The current state of the law in Australia
Whilst *Peak* remains the conventional wisdom on drafting guidance…

- The muddied state of the recent caselaw means the prevention principle is practically a fraught area for administration, advice and adjudication of disputes.
- The question of whether a time bar should be effective in displacing the prevention principle, rendering the contractor liable for not only delay costs, but also liquidated damages is a current controversy in construction law.
Recent cases…

• *Turner Corp v Austotel* (1997) 13 BCL 378
  – The contractor had claimed an extension of time for principal-caused delays which the principal granted. However, the contractor had further argued that the owner’s right to LDs for other delays had also been lost as a result of its acts of prevention.
  – Cole J held that the concept of prevention did not apply because an appropriate EOT had in fact been granted.
  – At 384-385 he states, in obiter, that a time bar should be effective in displacing the prevention principle.

  – Rolfe J held that the delays by the principal were “concurrent” with the contractor’s delays and did not result in an actual delay to the work of the contractor and thus the concept of prevention and time being at large did not apply > contrary to the formulation of PP in *Peak.*
Recent cases…

- **Gaymark v Walter** (2000) 16 BCL 449
  - Principal assumed *Peak* risk through injudicious amendments to standard form, removing unilateral power to extend time. Bailey J held the prevention principle to apply where the contractor is time barred.
  - Came under fire from the late Professor Ian Duncan Wallace, QC and in *Multiplex Constructions v Honeywell (No 2)* [2007] EWHC 447.
  - Notwithstanding this criticism, it remains the only case that expressly decides whether a time bar should be effective in displacing the prevention principle.

- **Peninsula Balmain v Abigroup** (2002) 18 BCL 322
  - Hodgson J identified the potential nexus between AS 2124 c11 23 (superintendent) and 35.5 (EOT) => the principal must ensure the superintendent acts honestly and fairly and, in doing so, exercise its unilateral power to extend time for the benefit of both parties.
  - His Honour found the unilateral power could be exercised retrospectively, even if the superintendent failed to do so, to prevent the operation of the prevention principle and time being set at large.
  - Superintendent failed to do so => principal loses right to some LDs.
  - At [78], in obiter, Hodgson J cited *Turner* cases favourably, undermining *Gaymark*. 
Recent cases…

• *Hervey Bay v Civil Mining and Construction* [2008] QSC 58
  – McMurdo J upheld the efficacy of the following amendments, breaking the potential nexus between AS 2124 cll 23 (superintendent) and 35.5 (EOT):
    1) Adding: “in the Superintendent’s absolute discretion and without being under any obligation to do so” to the relevant part of the EOT clause
    2) Adding a “Conditions Precedent to Extension of Time Claims” subclause to the EOT clause
    3) Adding to the relevant part of the Superintendent clause: “the Principal and Superintendent may exercise those discretions and rights given to them under the Contract in whatever way the Principal or Superintendent decide in their absolute discretion”
  – Amendments along these lines have been common in amended AS contracts since *Peninsula Balmain*
  – *Peninsula Balmain* approved but distinguished

• *Spiers Earthworks v Landtec* (2012) 28 BCL 282
  – Trial judge applied *Peninsula Balmain* to grant a 42 day EOT
  – On appeal the Contractor said it did not seek an EOT but sought to have time set at large
  – Appeal dismissed
Academic opinion

• In his article ‘Can Prevention be Cured by Time Bars?’, Professor Doug Jones makes a compelling argument for the prevention principle defeating time bars noting Gaymark remains the only case that expressly decides whether a time bar should be effective in displacing the prevention principle.

• In his article ‘Prevention and Liquidated Damages: A Theory Too Far?’, Professor Ian Duncan Wallace echoes the sentiment of Cole J and Rolfe J in the Turner cases and heavily criticises the Gaymark decision.
Determining a liquidated damages claim in an adjudication
My adjudication: the facts…

- The contract in question was between a main contractor ("MC") and subcontractor ("SC") and consisted of a bespoke short form subcontract agreement and attachments.
- The Works consisted of, *inter alia*, demolition, earthworks, concrete, trenching and conduit and pit installation.
- Relevantly, the subcontract provided:
  - a contract price of $1,394,070.82.
  - a date for practical completion of 17 August 2015.
  - by clause 17, if SC failed to achieve practical completion by the date for practical completion it would be liable to pay liquidated damages.
  - a liquidated damages regime of $35,000 (exclusive of GST) per calendar day up to a maximum of $350,000 (exclusive of GST); and
  - by clause 28, MC was entitled to set-off amounts for monies owed by SC to MC.
- There was no superintendent.
- The Works were on the critical path of the main contract schedule.
The facts…

• SC achieved practical completion on 28 October 2015, 72 days after the date for practical completion.

• In a letter dated 4 December 2015, the Principal (“P”) notified MC that:
  – the main contract date for practical completion was 21 September 2015;
  – MC achieved practical completion on 28 October 2015, resulting in a 31 day delay; and
  – P had elected to set off liquidated in the amount of $351,361.87 from MC’s November 2015 payment claim.

• By email dated 8 December 2015, alleging SC was responsible for the delay, MC levied LDs of $350,000, the maximum amount possible under the subcontract, in liquidated damages against SC.

• By email dated 18 December 2015, SC submitted its delay damages claim, V10, which showed 42 alleged MC caused delays (acts of prevention).
My assessment of the delays

• SC’s delay damages claim alleged 42 MC caused delays which came to 126.4 days in total
• I found there to be at least 104 days of MC caused delays which were on the critical path and were not concurrent
• In the response, MC did not provide any evidence to suggest Swan had not attempted to mitigate these delays
• I was satisfied, on the balance of probabilities, that MC caused delays to completion of the Works in excess of Swan’s 72 day over run
The subcontract EOT clause

The Sub-contractor shall promptly, and in any event **within 2 working days of its occurrence**, notify the Main Contractor of any delay which may affect the Completion Date stated in the Agreement. If the completion of the Works is delayed through any act or omission of the Main Contractor its employees or agents, the Main Contractor **may grant a reasonable extension of time**, but shall be under no obligation to do so if notification of delay has not been made as herein provided.
The response

• MC cited *Turner Corp v Austotel* in support of its contention that the prevention principle could not operate under the subcontract.

• To address this submission, I:
  – noted the views of Cole J on whether a time bar should be effective in displacing the prevention principle, although persuasive where expressed in obiter; and
  – referenced Professor Doug Jones article, ‘Can Prevention be Cured by Time Bars?’ and *Peak* at 121 in support of the proposition that LD clauses should be interpreted *contra proferentem*. 
MC’s implied obligation

• The subcontract was silent on whether MC was obliged to act fairly and justly when acting in the role of certifier
• Applying *Perini*, I found this obligation was an implied term of the subcontract
• In light of the apparent ambiguity between MC’s implied obligation to act fairly and justly and the express provision in the EOT clause that it is under no obligation to extend time if SC did not provide notification, the EOT clause must be construed *contra proferentem* (see *Peak* at 121)
• Consequently, MC’s obligation to act fairly and justly must prevail over the express provision that it is under no obligation to extend time if SC did not provide notification
Applying Peninsula Balmain

• MC’s overriding obligation to act fairly and justly compelled it to grant a unilateral extension of time if the completion of the works is delayed through any act or omission of MC

• Applying Peninsula Balmain and to prevent time being set at large, I was required to retrospectively extend the date for practical completion by 72 days, extinguishing MC’s liquidated damages claim

• I rejected MC’s liquidated damages claim
Summary of reasoning

1) A principal’s act of prevention causes delay to critical path

2) Delay is not concurrent with contractor delays (contrary to Peak, but consistent with Turner – err on the side of caution)

3) Unless expressly excluded, certifier (usually superintendent) has obligation to act justly and fairly (see Perini)

4) In the event of ambiguity, EOT / LDs clause to be construed contra proferentem (see Peak at 121)

5) EOT clause must have unilateral power to extend time in the event the contractor does not request EOT otherwise prevention principle will be enlivened (see Peak and Gaymark)

6) The superintendent must exercise its unilateral power to extend time, as per Peninsula Balmain, unless the contract contains Hervey Bay type amendments
In closing…

My determination is the subject of an application for judicial review so it will be interesting to see how my reasons stand up to the scrutiny of the WASC…
Questions?