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Onerous Contract Provisions

Introduction

There is an imbalance between the rights and obligations and hence liabilities and risks, borne by sub-contractors as against contractors.

Risk is increasingly being shifted onto the sub-contractor ignoring the fundamental principles of good risk allocation being that:-

- Risk should be allocated to the party best able to control it, and
- Responsibility for risk should be matched with appropriate authority and proper reward.

This imbalance and its associated consequences is a flavour which flows through the whole of the contract process from tendering, to bidding, bid shopping, the contract terms themselves and its administration based on those terms.

The question for the specialist trades and those advising them is, how do we best address and overcome these problems? In truth, I believe the only true answer lies in legislative reform. But, there are other things we can do too. The purpose of this paper is to explore what these options are and what we, as participants in the sub-contracting industry, can do about it.

Has BCIPA helped?

Most of us would agree BCIPA has been a great help to the sub-contracting industry. It has certainly helped improve cash flow but there are two significant problems with it.

The first is that to some extent, it has precipitated the big end of town to bring in even more nasty and onerous terms of contract than were seen previously. One example of this is the extremely short time frame sub-contractors are given to do things under contracts nowadays in almost all of the contracts for major builders.

The second problem is that BCIPA only helps with what we as lawyers call "the back end".

That is, it deals with payment problems once they have arisen.

It is true that BCIPA prohibits "paid if and when paid" clauses and so on but it does very little to help with "front end" problems emanating from nasty or onerous terms and conditions and builder conduct.

What causes these onerous or nasty contract provisions?

The big end of town will tell you that the reason terms and conditions imposed on sub-contractors are much harsher than those imposed on the contractor/builder are:-

- The principal only has to worry about one contract whereas the contractor has to worry about multiple sub-contractors and it therefore needs to be tough on them all to make sure the contractor/builder keeps control;
- The contractor cannot put in his Payment Claim or Progress Claim until such time as he has all sub-contractors' claims. The contractor is therefore justified in imposing short and strict time limits within which sub-contractors must put in claims and do other things under the contract. Otherwise, the argument goes, the builder/contractor will have insufficient certainty to know what he is to do under his contract with the principal;
- The alleged low level of administrative expertise amongst sub-contractors, means the builder/contractor has to be very specific about what and when the sub-contractor is required to do. Hence, strict and very specific provisions in the contract.

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The reality however is that most of these reasons are nonsense.

There is only one real reason why the big end of town insists on trying to impose such harsh contract terms on sub-contractors. That is, they believe they have the economic power to force you to take whatever you are offered.

Examples of some onerous contract provisions

They are many and varied. The regular offenders however seem to be clauses such as the following:-

Extension of time

The time frames within which EOT claims must be made have come down dramatically in recent years, particularly since BCIPA. The level of detail required to be put in a claim has also been increased. If you only have three to five days to make an EOT claim, how realistic is it then for you to provide a detailed breakdown of the costs, causes, estimated length of delays involved and what you plan to do to overcome the delays?

Furthermore, when an extension is granted, as often as not, that does not entitle you to any compensation for the extra costs incurred and sometimes that is so, even where the builder/ contractor is the cause of the delay.

Commonly, if you do not provide all that information within that limited time frame, you are barred from making a claim.

Obligation to accelerate without compensation

These clauses oblige the sub-contractor to accelerate his works if so directed but allow no compensation for any extra costs incurred as a result. This is commercially unrealistic.

Variation claims

Again, the time frames within which you must make a claim for a variation have become increasingly short...down to a matter of a few days. Notwithstanding that, you are commonly required to give full details not just of what it is your claim is about but also the "legal basis" upon which the claim is based and that includes whether based on a term of the contract or some other legal principle such as an equitable claim. How many sub-contractors are in a position to do that in such a short period of time (or even their lawyers for that matter)?

Delay claims

The right to claim damages for delays such as inclement weather or industrial action are under threat. You are now sometimes deemed to have taken into account any such delays in coming to your price and time for completion of the project. This is simply unrealistic.

No collusion

Some contracts seek not only to prohibit sub-contractors from colluding with other tenderers (which is illegal anyway under the Trade Practices Act) but also from communicating in any way with your association or with an association of which you are not even a member but of which another tenderer might be a member. How are you supposed to know that some other tenderer is a member of an association? If the prohibition was for the purpose of preventing collusion, again that would be acceptable but an absolute prohibition which would prevent a sub-contractor obtaining useful information from its association which may assist it with the tender process (such as a legal opinion provided to the association for its members on the terms of a tender) goes too far and is not reasonable.

Restrictions on key people

Contracts now provide that you cannot take a key person off the job or replace them with someone else without the builder/contractor or the project manager's consent. Surely if you have won the job it is up to you to perform the contract and if you fail to perform the contract adequately, the builder/ contractor has its remedies.

Indemnities

Most contracts from "the big end of town" are now littered with provisions under which the sub-contractors indemnify the builder/contractor for all types of losses.

For many of these, you cannot be insured.

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What is worse, some contracts even provide that the builder/contractor is not liable for any costs which the sub-contractor incurs even where it is the result of negligence on the part of the builder/contractor. That defies hundreds of years of accepted legal principles and is also uninsurable.

"Design coordination problems" and inadequate "work descriptions"

In many contracts, if there is a problem arising from the design, yours or design work done by someone else, or the work description has left something out, it is your responsibility to overcome the problem and absorb any costs caused by the problem. This is notwithstanding that the design failures may have been the design failures of the builder/contractor, the principal or their consultants such as hydraulic consultants or mechanical engineers. How can it be reasonable for a sub-contractor to be given the contractual risk and responsibility for rectifying mistakes made by specialist consultants? These types of clauses are inevitably linked with prohibitions on the sub-contractor making any claim in relation to any such failure by the consultants, builder/contractor or principal.

Prior works warranty

Sub-contractors are being asked to warrant that prior to carrying out work on a part of the site where other trades have already carried out works, are "suitable" for the sub-contractor to do their work. Why should a following trade carry the responsibility and potential liability of effectively certifying that something another trade has done was done properly? Is it not the job of the builder/contractor or the project manager or whoever the superintendent is, to ensure this?

Intellectual property transfers & warranties

Contracts regularly provide that you warrant that you own all intellectual property used in the works. Often you do not. Further, they commonly provide that you assign all your rights in such intellectual property to the builder/contractor. You can't if you do not own it. You may also be signing away much more than you think including intellectual property you value and do not wish to give away.

Moral rights

Contracts usually require sub-contractors to indemnify the builder/contractor against any liability it may suffer as a consequence of some breach of the moral rights of a person such as one of your employees. I do not so much think this unfair but know that many sub-contractors do not adequately cover off against this risk in their employment contracts, as they really have to given that claims of this type can be substantial.

Set offs

Contracts commonly allow the builder/contractor to set off any money you may owe them under some other contract against moneys they owe you under the subject building contract. Strangely enough, a reciprocal right allowing you to do the same, is never included.

Right to vary down scope

Clauses which allow the builder/contractor to vary the scope of your works without limitation are common and can and are misused. In a case I had a year or so ago, a principal sought to vary down the scope of works to almost zero using such a clause. Our opinion is that such broad clauses used in that way may not work but regardless, it places the sub-contractor in a very difficult position it if is done to him.

Defects rectification by third parties

Some contracts provide that during the defects liability period, the builder/contractor can have a third party carry out defect rectification without even giving you prior notice or an opportunity to attend to it yourself. At the same time, the builder/contractor has the right call on your bank guarantee or your retention moneys.

The retention moneys are there as security against the risk of defects you do not recitify, not to fund someone else to do work.

Compulsory dispute resolution before Payment Claim

The insertion into a contract of a clause mandating participation in a dispute resolution process before you have a right to lodge a Payment Claim under the BCIPA can be used to slow down your cash flow and increase your legal costs. In turn, this puts more pressure on sub-contractors to resolve disputes by giving up justifiable claims.

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That said, if the process is too convoluted and will take too long, such clauses can be struck down. The question is however, do you really want to go to court to do so?

Seizure of equipment

A right to seize your equipment to pay moneys allegedly owing to the builder/contractor, is occasionally included. Usually one needs a judgment before you can enforce a claim for payment. However, by a clause like this, you are effectively contracting to give the builder/contractor a right of execution before determination of any dispute.

Proof of "financial robustness"

These type of clauses entitle the builder/contractor to give notice that they require the sub-contractor to provide proof, satisfactory to the builder/contractor that the sub-contractor is "financially robust". Further, if such notice has been given, the right to lodge a Payment Claim or seek a valuation of works is suspended until such evidence is provided to the satisfaction of the builder. This is just another tactic that can be used to delay payment and another hurdle which you have to clear before you can serve a Payment Claim and use BCIPA.

Right to inspect your records

A clause which gives the builder/contractor the right to inspect your records at any time, could be used against a sub-contractor in unexpected ways. Many of them are drafted so broadly that the builder/contractor could use them during a dispute to gain access to documents they are not otherwise entitled to. Again, strangely enough a reciprocal right for you to do the same to the builder/contractor is never included.

Termination for insolvency

Nobody would object to a right in the contractor/builder to terminate the contract in the event of a sub-contractor's insolvency. However, "insolvency" is being defined more and more as a question of arbitrary opinion of the builder/contractor. I have recently seen a contract in which "insolvency" was defined to include where the builder/contractor "reasonably forms the view that the contractor is insolvent".

Release upon claim made

Clauses which provide that upon submitting a Progress Claim or a request for valuation (which ultimately leads to a RCTI being issued) constitutes a bar for any further claim for any prior work, can leave the sub-contractor out of pocket for expenses incurred on a job but which have not yet been billed to the sub-contractor by the supplier for example. It is particularly concerning where contracts contain such a provision with respect to final Progress Claims and under which, the sub-contractor is deemed to release the builder/contractor by the mere act of having made a final Progress Claim or submitted a request for valuation for a final Progress Claim. These clauses commonly also seek to rule out any type of legal action whatsoever by the sub-contractor in relation to anything that has occurred prior to that date. Notwithstanding that, they never seek to prohibit the builder/contractor from making a claim against the sub-contractor in relation to any such prior work.

Payment of deposit before can sue

We have even seen contracts where before the sub-contractor can take action (court, dispute resolution or otherwise) against the builder/contractor, the contract requires the sub-contractor to pay a sum equivalent to ten percent of the amount proposed to be claimed to the builder/contractor. Signing a clause like this is effectively granting security for costs to the builder/contractor without a court order.

Stat Dec's and releases

You will all be familiar with clauses requiring you to submit a statutory declaration with your Payment Claim or request for valuation to the effect that you have paid all your workers, sub-contractors and even your suppliers. Some even require you to declare that your sub-sub-contractors and your suppliers have paid their staff. How many of these statutory declarations are made falsely or without any real knowledge as to the truth of the facts? I shudder to think. However, failure to provide such a statutory declaration prevents you being paid and is a contractual requirement which must be complied with before you can deliver a Payment Claim under BCIPA. If you falsely stated in a statutory declaration that someone had been paid and the builder/contractor was able to prove that to be untrue, your Payment Claim could be invalid.

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Termination for inadequate progress

The concept that a builder/contractor should be entitled to terminate a sub-contractor's contract because they are holding up the works generally is fair and reasonable. Clauses which give that right where the sub-contractor fails to comply with a Project Program are also reasonable provided the builder/contractor cannot unilaterally change it (as they commonly can). However, clauses (which are increasingly common) to the effect that a builder/contractor can terminate the contract simply because the builder/contractor does not consider the sub-contractor's progress to be "satisfactory" without any reference to any objective criteria, is simply unreasonable especially in circumstances when reference to the Project Program could be made. Such clauses are an open opportunity for the builder/contractor to terminate your contract without true or fair cause.

Termination for convenience

Basically these clauses mean you have a contract for so long as the builder/contractor wants you to have one. They are just about as unfair a term of contract as could be imagined. What is worse is that if they are relied on to terminate your services, you are usually not entitled to any claim for loss of profits – something completely inconsistent with common law principles.

Wrongful termination deemed to be for convenience

This is about as bad as it gets! I have seen a clause where a termination by the builder/contractor, if found by a court or arbitrator to have been wrongful, is deemed to be a termination for convenience. This means that even if the High Court of Australia finds that there has been a wrongful termination of contract by the builder/contractor entitling a sub-contractor to millions of dollars of damages they will not get it because they have agreed, by signing the contract, to accept that any wrongful termination, no matter how unjustified or unfair that was, was "a termination for convenience" merely entitling them to be paid for the work they had done prior to termination of the contract and for some de-mobilisation costs.

Just how much are sub-contractors prepared to sign away before they do something to stop this rot?

What other related problems make life tough for sub-contractors?

Other problems I have seen in recent times, include the following:-

- **Bank guarantees not being given back when they should.**

  Contracts sometimes do not place a clear obligation on the contractor to release the bank guarantees when they should. This is exacerbated by sub-contractors not standing up for their rights and insisting that bank guarantees be given back by seeking a mandatory injunction. This is no doubt partly because of the legal costs involved;

- **Generally, sub-contractors not being prepared to fight for their rights.** This seems to me to be because they do not believe they will ever be able to have any terms changed and they are worried that the builder will just go to the next sub-contractor who is more compliant. That's not necessarily the case;

- **Sub-contractors are not even asking for onerous terms to be altered**. This is a big problem and an attitude in the sub-contractor industry which needs to change if there is to be any progress;

- "**Bid Shopping**". How common is it to see that tenders are called, tenders put in, the contractor/builder is awarded the contract and then he comes back trying to get you to reduce your tender or, just as bad, he shops your tender around to others seeking a lowest price based on your tender and your design savings;

- **Sub-contractors not complying with the contractual requirements**. A typical example would be where a notice or claim is required to be done within a certain time frame and it is not followed.

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Remember, that if the contract says you have to submit your invoices on pink paper with photographs of elephants around the edges, you have to do it. Until such time as you comply with the contractual terms, you cannot enforce your rights under BCIPA (and will not be able to do so in the ordinary courts either);

- **Sub-contractors are simply not using BCIPA** because they are scared of the contractor/builder;

- **Sub-contractors are not using the *Sub-contractors Charges Act*** for the same reason.This is even more of a concern because usually the reason you are considering using the Sub-contractors Charges Act is because the builder looks like going broke or you have severe doubts about their financial capacity to survive.

So what can sub-contractors do to address this imbalance?

"Don't submit a tender unless you fully understand and accept the terms of the proposed contract"

I have lost count of the number of times sub-contractors have come to us and asked us to look over a contract after they have been awarded it. While some times you are able to negotiate changes to the contract after you have been awarded the contract, it's basically too late as the builder has you by the proverbials at that stage, especially if you are already on site. You need to look at the terms of the contract as part of the tender analysis process.

If you put in a tender it will be taken as a matter of law to be a price based on the terms of contract contained in the tender documents. So, when you get the tender, look at the terms and conditions of the contract and try to negotiate any required changes then.

If you cannot get the builder/contractor to participate in that process at that time (as is often the case), when you put in your tender, put it in on the basis that clauses 16, 32 or whatever they are, being the clauses you object to, are to be deleted and replaced with new clauses on terms acceptable to you.

I accept that this may reduce your prospects of being the successful tenderer but too many sub-contractors are currently taking a punt by putting in prices on terms which could be used to ultimately bring about their financial ruin.

You have to be able to recognise unfair provisions

Someone who knows what they are doing has to read the tender, including the contract. There is plenty of experience and knowledge in your industry and usually, this should mean that if an appropriate person in your organisation sits down and reads the contract properly (and the other tender documents) you will know what the problem clauses are.

However, not every company has the relevant expertise. Secondly, there are increasingly what I call "tricky little legal bits", in these contracts which may not be apparent to many who are not lawyers. One possible solution to help with this might be that when new big job tender documents come out, your associations could brief a law firm to provide it with an advice on the contract identifying the nasty provisions and making recommendations for their amendment.

Your association would pay a fee for this but would recoup its money (and probably more) by on-selling this advice to its members. If an advice were to cost $6,000.00 plus GST and the advice was , by this mechanism, "sold" to twelve contractors, that would mean each contractor would only be paying $500.00 plus GST for a decent legal analysis of a major contract, pointing out the nasties and recommending changes.

From there, each sub-contractor who buys the advice can make a decision what they are going to do. They can give that to their in-house counsel if they have one or to their external lawyers or simply use it to make decisions about what they will and will not wear, in terms of nasty or onerous conditions.

One warning on this of course, is that this process would have to be carefully managed so as not to offend the provisions of the *Trade Practices Act*.

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Try negotiating

Once you have identified the nasty clauses and how you would like to change them, you need to have a meeting, face to face with the contractor/builder to sort it out. I believe that you are often better off trying to get them to bring their lawyer (but to attend the meeting without yours). That of course is on the proviso that you do not officially sign off on anything and ensure that at the end of the meeting, you have an agreement subject to you checking things with your lawyer.

I have several reasons for suggesting this. The first is because you might get all you want without your lawyer there. If you do, it will be cheaper. Secondly in my experience, and many of you may not like what I say, I have found lawyers (even those representing builders/contractors) to be more reasonable than their clients, especially the big end of town.

I think their lawyers are actually a moderating influence on their clients but acknowledge that is certainly not always the case.

For the same reasons, I think where possible, if you are emailing back and forth with the builder about terms and conditions or some dispute, you should try to cc their in-house lawyer or external lawyer, as the case may be.

Doing this creates pressure on the person you are dealing with (the project manager or whoever) to take legal advice. If things go "balls up" from their end there is a real prospect that the person who decided not to take legal advice is going to be asked, "Why didn't you check with the lawyers before you agreed to that or before you refused to agree to that?"

There is only one place better than a major corporation for what is politely referred to as "covering one's backside by having the lawyers sign off" and that is government departments. Try it.

Comply with the terms of the contract

Make sure you read the contract and know what it requires. Make sure you comply with the time limits and all the procedural hoops that have to be stepped through. If you do not, the builder will not pay you or will not accept your claim. If you then dispute it, you will lose.

Use BCIPA

What the big end of town often does is ambush the principal, usually toward the end of the job, by a massive BCIPA claim. As they go through the project, they document all the little disputes and differences they have had with the principal and have it more or less ready to go, to be all included in one Payment Claim at the end of the job or near to it.

This can result in a very large, in terms of dollars and paperwork, Payment Claim being delivered to the principal. Their project managers, engineers and lawyers then only have ten business days within which to respond with a Payment Schedule. Remember, if anything is left out of the Payment Schedule, it can't subsequently be argued in adjudication.

If you think that's tough, remember this is likely to mean the poor old adjudicator (like my associate Michael Cope of McKays), will end up with an adjudication of 10-20 lever arch folders from the applicant and just as many from the respondent, which he not only has to read but also to consider the issues dealt with in them and make decisions in relation to them, all within ten business days.

Some of you will no doubt already do this but for those of you who don't, I think it would be well worth your while considering adopting this tactic yourself and documenting your potential claims as you go.

Use pre-bid agreements

In order to reduce the risk of your tender being used to bid down other tenderers and vice a versa, you should endeavour to have the contractor/builder agree in a formal document that your tender is submitted on the basis that it and the price is confidential between the parties and if you are the successful tenderer the contractor **will** enter into a sub-contract with you on the terms contained in the tender (as amended with your requested changes). If you have no chance of the builder/contractor signing something to that effect, put it in your covering letter under which you submit your tender.

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Be warned however, that depending on the terms of the tender you might be rendering your tender non-conforming. Check carefully.

What legislative solutions may there be?

"Ban bid-shopping"

I think it is time that we gave serious consideration in this country to outlawing "bid shopping".

In some foreign jurisdictions, California being one example, they have legislation banning bid-shopping. See the Californian *Sub-letting* and *Sub-contracting Fair Practices Act*.

As I understand that legislation requires builders to "list" in their tender with any public agency, the names of each sub-contractor who will perform work in excess of one and half percent of the total builder's build price. The contractor must also specify what works each sub-contractor is going to do and cannot, at least not without severe penalty, subsequently use some other sub-contractor except in certain special cases such as where the sub-contractor has gone broke or refuses to sign the contract.

There are case authorities in these jurisdictions confirming that a sub-contractor who, in breach of the listing requirements, is subsequently not awarded the contract, can sue for loss of profits.

I suggest this type of legislation should be on our agenda.

Sub-contract terms not to be substantially more onerous

Another possible legislative reform would be for the state governments to legislate that sub-contracts cannot be on substantially more onerous terms with respect to a series of listed issues, than the contract between the principal and the contractor. The types of issues which this should apply include but are not limited to:-

- Extensions of time – the time frames and rules given in head contracts for extensions of time, should be reflected in the sub-contracts;
- Delay damages claims – again, the two contracts should reflect each other. For example, if the head contract allows the builder/contractor to delay damages for industrial action and inclement weather so should the sub-contracts. Similarly, if the principal contract does not seek to limit delay damages to two bob fifty a day, nor should the sub-contract be allowed to;
- Variation claims – if a principal contract allows the builder/contractor to put in a variation claim "within a reasonable time" the sub-contract should also. Currently, it is more common to see provisions to the effect that a variation sought by a sub-contractor must be made within three to seven days of the sub-contractor becoming aware of the need for a variation;
- Termination for convenience – if the principal contract provides that if there is to be a termination for convenience, the principal is to pay the builder/contractor compensation including for loss of profits, so should the sub-contract. In my personal view, I think termination for convenience clauses are a disgrace and should be unlawful (execpt possibly in the case of a change of government);
- Other grounds for termination – those in the sub-contract, should not be more extensive than those in the head contract.

Outlaw unfair terms

We should be looking at encouraging the government to legislate in a way similar to that which it has already done in the *QBSA Act* by imposing statutory time limits for the making of variation claims and extensions of time, giving notices under contracts etc, banning termination for convenience clauses etc. However, the *QBSA Act* does not cover everyone in the industry. One example is electrical contractors. Such laws should cover everybody.

The bad news is that this could be difficult to do, including at a political level. You will however have something you can fight with, if rules such as these were brought in.

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Other options

I know David McAdam has raised as a possible part solution some sort of dispute resolution process about the "reasonableness" or otherwise of terms in a contract perhaps using an adjudication process similar to that under BCIPA or indeed, extending BCIPA for that purpose.

There is in fact a precedent for this type of approach in the *Legal Professional Act*, that is the legislation that governs the duties and obligations of lawyers including costs they can charge.

Under section 328 of the *Legal Professional Act 2007*, a lawyer's client can apply either to the Supreme Court or QCAT for an order that a costs agreement entered into between the client and the law firm be set aside as "not fair and reasonable" even well after the work has been completed. If it finds that it is not, it can then effectively re-write the contract and change the level of costs payable to the lawyer.

An extension of the BCIPA along the lines David McAdam has suggested would be placing a lot of power in the hands of adjudicators. It would have the benefit of merely being an extension of an existing and reasonably well understood system (and possibly therefore easier to get through, politically). It could also be quick and relatively inexpensive. On the other hand the "a rough justice" approach like that taken in adjudication proceedings already, may not necessarily be in the best interest of the parties. Perhaps it should be another new turf for that all encompassing lawyers' horror, QCAT.

The certainty provided by legislative intervention of the types referred to above would in my view, be preferable but it may be a question of what can and cannot be done politically.

Conclusion

I have sought to outline in this paper what I think are some of the problems and solutions which the sub-contracting industry faces. I have set out a number options available to the sub-contracting industry ranging from "self help" type options to legislative solutions.

In conclusion, I think all these options need to be utilised if a degree of fairness and reasonableness is to be restored to the relationship between sub-contractors and builders/contractors.

The big end of town will never stop inventing new ways of trying to gain the advantage as is their commercial right.

We do however live in a society which accepts that legislative intervention is appropriate where the actions of some adversely affect the rights and livelihoods of others.

In my view, the time has certainly come for there to be legislative intervention and perhaps along several lines.

That however, cannot and should not relieve individual sub-contractors from standing up for their rights and making sensible business decisions by not accepting terms and conditions of contracts which could lead to their ultimate, financial collapse as many of them currently risk.

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