Construction Contracts after MT Højgaard

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What can be learned from the Supreme Court's ruling in *MT Højgaard AS v E.ON Climate and Renewables UK Robin Rigg East Ltd?*

A significant outcome from the case has been a raised awareness and increased reluctance on behalf of designers to enter into contracts containing fitness for purpose obligations.

And who can blame them, given the titanic difference between their consideration and the potential liabilities entailed?

Take the example of a harbour wall. The designer's fee, at most, will barely run into the six figures, while the liability for this collapsing on a commercial vessel would run into the millions. Consider the outcome if an oil tanker, which subsequently spilled, was involved.

You can see why it may be difficult to obtain insurance for such potentially high value unknowns and why designers would be reluctant to accept such liabilities. Especially, since they could be found liable for defects caused by errors in the recognised standard – as was the case in Højgaard.

This case highlights the importance of understanding the contractual requirements placed on designers. The headline issues are:

Process v Outcome

There are two main categories for obligations a designer can be required to meet. "*Process*" obligations commonly require compliance with required standards or specifications and the exercise of reasonable skill and care of a qualified professional when doing so. While "*outcome*" based obligations are strict obligations to achieve a required outcome or a fit for purpose requirement.

Designers are more comfortable with process requirements because the edges of their liability can be determined, and they can obtain insurance more easily. In contrast, Employers are more likely to prefer outcome-based obligations to achieve certainty of performance and the straightforward proof of non-conformance resulting in the ability to

claim for remediation costs.

The key point for all parties is clarity, as the court has indicated that twin obligations (compliance with a standard and a fitness purpose requirement) are enforceable. However, a fitness for purpose obligation may be reduced if the contract also contains reasonable skill and care obligations and the relationship isn't clear. It's therefore easy to see the benefit of ensuring that the obligations imposed, and their relationship is clear and that there is an express order of priority. This avoids the reduction issue for Employers while allowing Designers to accurately access requirements.

Fitness for purpose

In *Højgaard*, the Supreme Court adopted the general rule from a Canadian Case (*Great Vancouver Water District v North American Pipe and Steel Ltd*) regarding the supply of water pipes found to be unfit for purpose. Despite being manufactured according to the specification set, they were deemed to be not fit for the purpose stated and the rule was established that:

> *"defects caused by an owner's specification are not the responsibility of the Contractor, unless the contractor expressly guarantees that the construction would be fit for a specific purpose, or a warranty can be implied by the owner's actual reliance on the contractor's skill and judgment".*

You can then see how, in a contractual situation with outcome requirements, a designer might find itself in hot water despite following the employer's specifications to the letter. Similar to *North American Pipe*, *MT Højgaard*'s designer was liable for the failure of wind turbines despite the fact they had been designed in accordance with the specification stated. The specification contained an error in the calculations for grouted connections resulting in foundations significantly weaker than required to be fit for purpose.

Once again, the key is clarity and the careful consideration of design obligations when drafting or reviewing contracts.

Standard Forms and Fitness for Purpose

Something to be aware of is that fitness for purpose is by no means a new requirement. Under most contracts, the default requirement is to ensure that the finished works are fit for the purpose stated.

In *Young & Martern Ltd. v McManus Childs,* a sub-contractor fixed roof tiles with an undetectable defect causing them to disintegrate within a year. The court ruled that in the absence of any express terms in a contract, any goods or materials supplied by a Contractor will be reasonably fit for the purpose for which they are supplied. This common law principle includes construction works and design where the purpose is made known to the Contractor, who has held themselves capable of providing such works. This is also the position under the Sale of Goods Act where a purpose is made known.

The NEC suite of Engineering & Construction Contracts require the use of Option X15 to limit liability to reasonable skill and care. This indicates that the common law position applies by default. It should be noted that the Works Information can expressly state either requirement. Ireland's Public Works Contract ("*PWC*") places fitness for purpose requirements both on the design and construction of Works.

In contrast, The NEC Professional Service Contract ("*PSC*") contains an express term at Clause 20.2 (NEC 4) or Clause 21.2 (NEC 3) which limits the consultant's obligations to reasonable skill and care. Aside from placing the more onerous requirement on the Contractor, this has implications for Contractors when employing a designer under the unamended PSC, as the standard of care obligations are not back to back. As such, a Contractor may find themselves liable to the Employer on an outcome provision but unable to claim from their designer who is only obligated to meet process requirements. Designers should also consider this and be wary of any amendments to these clauses.

Design liabilities in JCT's Design and Build contracts are by default limited to the reasonable skill and care standard whereas an unamended FIDIC contract will contain an express requirement to be "*fit for the purposes for which the works are intended.*"

Parties also need to be aware of "*stealth*" fitness for purpose amended clauses which add strict liability requiring "*suitability for the purposes stated*" or a similar wording.

The message here is to be sure that you know the standard of care required of any contracts considered, to check that any sub-contracts pass these down and ensure that appropriate insurance is in place.

Conclusion

In complex and likely multi-authored construction contracts, inconsistencies are highly probable and without thorough assessment it can be easy to overlook onerous fitness for purpose obligations.

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