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LAWYERS

FERTILE GROUNDS FOR DISPUTE Site conditions and the exclusion of liability

Introduction

It is a truism in the construction industry that it is preferable for risks to be allocated to the party who is best able to manage or control those risks. However, this will not always be possible in the case of unknown site conditions, or 'latent' conditions, perhaps because it is difficult to determine who should bear responsibility for circumstances over which neither party to a contract is likely to have special knowledge or control.

The many variables involved in the discovery of latent conditions also serve to increase uncertainty in this area, as the effects of unexpectedly adverse site conditions may be wide-reaching. The works may have been planned on the basis of certain assumptions, and the discovery of unexpected conditions may necessitate changes to work methods, the design or the works as a whole. As a result, the works may be subject to significant delay and increased costs.

Most commonly, the contractor bears the risk that site conditions – whether geotechnical, contamination, asbestos, or otherwise – make the project more difficult or expensive to undertake than anticipated, taking into account information provided by the principal (if any). This update will look at the ways in which a contractor may nonetheless be able to claim the costs of dealing with latent conditions, even where the 'traditional' contractual risk allocation remains. On the other hand, from a principal's perspective, there are ways to help ensure that the contractually drafted risk allocation is effective to exclude any liability for latent conditions that may arise during the course of the works. These include the use of disclaimers, which are often incorporated into the site documentation given to the contractor during the tender period, as well as exclusion clauses, which may form part of the resulting construction contract itself.

Notwithstanding the legal principles which will be outlined in this update, the allocation of risk for unexpected site conditions will nevertheless turn on the specific circumstances of the case, making latent conditions a significant area for dispute.

Latent conditions claims

There are a number of mechanisms by which a contractor may attempt to recover the costs of dealing with latent conditions. Some contracts, including standard form contracts such as Australian Standard General Conditions of Contract AS 2124-1992, contain a dedicated latent conditions clause. Such clauses allow the contractor to claim the additional time and costs required to deal with latent conditions, where the conditions encountered were different from what should reasonably have been anticipated by the contractor at the time of tender. Alternatively, some contracts will permit a contractor to claim the additional time and costs through the contractual extension of time and variation provisions.

Even when the contract does not provide the contractor with any express entitlement in respect of latent conditions, there may still be avenues available to the contractor to recover some of its costs. For example, a contractor may argue that inadequacies in site information provided by the principal during the tender phase amount to misleading or deceptive conduct on the part of the principal, under the Australian Consumer Law. If successful, the contractor may be entitled to recover costs incurred as the result of reliance upon the site information provided (or not provided) by the principal, leading to a 'shift' in the allocation of risk, from the contractor to the principal, in respect of the cost of carrying out the work under the contract.

The fact that a contractor can bring a claim in respect of inaccuracies in site information may lead principals to consider that it would be safest to disclose as little as possible about the site to tenderers, and, indeed, it is common to see geotechnical or other site reports which are so equivocal or qualified that they provide little assistance in identifying the nature of the conditions to be expected. However, there are commercial and practical advantages in providing tenderers with available information to allow them to scope, price and program the work as accurately as possible. In addition, a failure to provide site information to which the principal has access may lead to allegations that the principal has engaged in misleading or deceptive conduct by denying the existence of that information, as was seen in the case of *Abigroup Contractors Pty Ltd v Sydney Catchment Authority* (2004) 208 ALR 630.

Disclaimers

Often, principals will try to avoid the risk of liability for errors in site information provided to the contractor during the tender phase by including a 'disclaimer' with that information, such as a statement to the effect that the information may not be accurate, or should not be relied upon by the contractor in formulating its tender. However, disclaimers will not always be effective in defending against claims of misrepresentation or misleading or deceptive conduct.

Some courts have reasoned that general disclaimers of liability should be of little weight in determining whether or not information supplied is misleading, on the basis that disclaimers are so common in commercial documents that a reader is not likely to take their presence as a particular indication that the information supplied is not thought to be reliable.

However, while a disclaimer clause cannot overcome the prohibition against misleading or deceptive conduct under the Australian Consumer Law, it seems that a disclaimer may be effective if the relevant clause actually has the effect of 'erasing' whatever would have otherwise been misleading in the conduct. A disclaimer is more likely to be effective if it relates specifically to the information being provided, rather than attempting to impose a broad and general qualification on the accuracy or completeness of the information.

For example, in the case of *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409, Pagone J considered that VicUrban had made clear that the relevant information was not presented as being accurate or reliable:

> [t]he so called "disclaimers" are positive information for the benefit of BMD rather than an attempt to disavow liability for what was being proffered for assistance. The context in which this was occurring is also important because the parties intended and understood that a contractor was being asked to assume a risk in undertaking a project and that VicUrban was informing BMD about the extent to which VicUrban was able to be of assistance in conveying information to BMD that might be useful…VicUrban took some care to inform BMD that it needed to ensure that the risk it was assuming was properly evaluated.

In the case of *Morrison-Knudsen International Co Inc & Anor v Commonwealth* [1972] 46 ALJR 265, contractors brought an action in respect of the Commonwealth's alleged failure to take reasonable care to ensure that tender information was accurate, following the discovery that, contrary to the information provided, the clays on the site contained large quantities of cobbles. In the High Court, Gibbs J, with whom Owen and Walsh JJ agreed, found that a disclaimer stating that the Commonwealth "would not be responsible for any interpretation or conclusion drawn by the Tenderer in regard to site conditions based on the information contained herein" was not actually a disclaimer of the information itself. In addition, the conditions which stated that the tenderer "shall have informed himself as to the site", and shall have "satisfied himself as to… physical conditions of the site" were not effective to exclude liability, as these clauses did not specify the sources to which the contractors should refer, or exclude the material provided by the Commonwealth. The disclaimers used by the Commonwealth failed to convey to the contractors that no responsibility would be accepted for errors or misleading statements in the information contained in the tender documents provided by the Commonwealth.

Exclusion clauses

Unlike disclaimers, which are generally made at the time that the site information is provided during the tender phase, exclusion clauses form part of the contract between the parties, and are intended to have the effect of limiting or excluding liability in respect of the matters specified.

The success of exclusion clauses in limiting or excluding liability for the cost of dealing with unexpected site conditions will depend to some extent on the nature of the claim brought by the contractor.

Generally, including in the recent High Court decision of *Selected Seeds Pty Ltd v QBEMM Pty Limited* (2010) 242 CLR 336, courts will interpret exclusion clauses narrowly, for the purpose of preserving the broader rights and obligations in the contract. In addition, where appropriate, exclusion clauses may be read *contra proferentem* in the event of ambiguity. This means that the clause will be interpreted *against* the party who originally proposed the clause, which, in the case of an exclusion clause which is ambiguous in its effect, is more likely to result in a finding that a particular type of liability is not excluded.

Importantly, in *Henjo Investments Pty Ltd v Collins Marrickville Pty Ltd (No 1)* (1988) 39 FCR 546, it was held that a contractual provision such as an exclusion clause cannot exclude liability for misleading or deceptive conduct under section 52 of the *Trade Practices Act 1974* (Cth), where misleading or deceptive conduct has, as a matter of fact, occurred. The recent Victorian Court of Appeal decision of *MBF Investments Pty Ltd v Nolan* [2011] VSCA 114 indicates that this principle will apply equally in relation to liability under section 18 of the Australian Consumer Law.

In addition, unlike a disclaimer, an exclusion clause is unlikely to be found to have the effect of 'erasing' misleading or deceptive conduct in the same way as might a disclaimer, as a result of the fact that the misleading or deceptive conduct will already have occurred by the time that the contract containing the clause is executed. For example, it could be argued that the misleading or deceptive conduct which induced entry into the contract also led the party to agree to be bound by the exclusion clause. Alternatively, there may have been an oral representation or promise which is inconsistent with the exclusion clause – in this case, the making of the representation may preclude a party from relying on the

exclusion clause in a way which would be inconsistent with that representation, and may also form the basis for a claim in contract or tort.

In relation to excluding liability for negligent misrepresentations, there has been some inconsistency in the authorities regarding whether the relevant exclusion clause must include an express reference to the exclusion of negligence, in order to successfully exclude or limit liability for negligence. While it now appears to be settled that an express reference to negligence is not required, it is nevertheless sensible to draft exclusion clauses in broad terms, and refer to the exclusion of liability for all types of loss, including negligence, to make clear that negligence was intended to be excluded.

Implications

Ultimately, whether or not a contractor succeeds in recovering in respect of the impact of dealing with unforeseen physical conditions will depend on the precise circumstances of the case, including the nature of the site information provided and the latent conditions encountered, as well as on the drafting of any disclaimers or exclusion clauses upon which the principal seeks to rely. Of course, the express contractual allocation of risk in respect of delay or additional costs arising from latent conditions will be relevant, although the cases discussed above indicate that this will not necessarily be determinative of the parties' respective rights and entitlements.

In this regard, it appears that where a principal is aware of particular limitations on the information provided in respect of physical conditions at the site, it would be well -advised to disclose those limitations in clear, written terms, at the time of making the information available, rather than seek to rely upon a broad and general exclusion of liability with respect to the tender information or as part of the contract terms. At the same time, however, a contractual risk allocation which requires the contractor to assume the risk of unforeseen site conditions may not be enforceable if the contractor is not provided with the information necessary to scope and price this risk, or given a reasonable opportunity to obtain it independently.

In each case, a principal will need to consider what is appropriate in the circumstances, taking into account these general principles. From a contractor's perspective, it is critical to review any such information provided by the principal, and ensure that material risks identified in respect of site conditions are addressed as far as possible in the contractual allocation of risk and pricing of the job.

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