International Arbitration Alert

Akin Gump
STRAUSS HAUER & FELD LLP

A Strict Approach to Notices as a Condition Precedent to Entitlement: The Impact for Contract Drafters and International Construction Arbitration

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Maeda Corporation and China State Construction Engineering (Hong Kong) Limited v Bauer Hong Kong Limited[1] handed down in the Hong Kong Court of Appeal has significantly elevated the fundamental importance of so-called 'time-bar' clauses (commonly seen in engineering, procurement and construction (EPC) contracts, International Federation of Consulting Engineers (FIDIC) forms of contract (e.g., Clause 20.2.4 of the Second Edition of the FIDIC Silver Book[2]) and many forms of international sub-contracts). The Judgement is important: It held that the sub-contractor could not pursue a claim in the arbitration where it had not raised the specific contractual basis of such claim in its 'time-bar' notice as required by the terms of the subcontract. Courts in common law jurisdictions will now be pushed to apply the 'pro-employer' jurisprudence in *Maeda Corporation* and arbitrators sitting in international construction arbitrations will be under tangible pressure to apply all 'time-bar' clauses strictly (even if there are draconian consequences for the 'non-compliant' contractor or sub-contractor).

Maeda Corporation considered a condition precedent clause that required the sub-contractor to state the contractual basis (together with full and detailed particulars and the evaluation) of its claim within 28 days after giving of its initial notice. The sub-contractor had not stated the same contractual basis of its claim as that advanced in arbitration. The question was whether the contractual basis of the claim made under the 'time-bar' clause had to be the same as the contractual basis of the claim made in the arbitration. The arbitrator decided that it did not placing significance on the commercial purpose of the condition precedent clause.

- The Court at First Instance held that it did and made clear "there can be no dispute, and no ambiguity, from the plain and clear language used in Clause 21, that the service of notices of claim in writing referred to in Clause 21.1 and 21.2 are conditions precedent, must be 'strictly' complied with, and failure to comply with these conditions will have the effect that the Defendant will have 'no entitlement' and 'no right' to any additional or extra payment, loss and expense."
- The Court of Appeal agreed with the Court at First Instance stating "Within the stipulated time, the Sub-Contractor is required to give notice of the contractual

Contact Information

If you have any questions concerning this alert, please contact:

Hamish Lal
Partner
hamish.lal@akingump.com
London
+44 20.7012.9740

Josephine Kaiding
Associate
josephine.kaiding@akingump.com
London
+ 44 20.7661.5356

Léa Defranchi
Associate
ldefranchi@akingump.com
Geneva
+ 41 22.888.2044

basis, not any possible contractual basis which may turn out not to be the correct basis. The reference to 'the contractual basis' would not preclude identifying more than one basis in the alternative or stating more than one basis in the notice or serving more than one notice each stating a contractual basis."

- *Maeda Corporation* will increase the number of condition precedent clauses that require the contractor or sub-contractor to also state the contractual basis of its claim; increase the focus on strict compliance with 'time-bar' clauses more generally; increase claims of waiver or estoppel made as a result of the way in which the parties had conducted themselves in relation to a claim notified under the 'time-bar' clause; and increase the use of 'in the alternative' notices issued by contractors or sub-contractors.
- Parties seeking to circumvent *Maeda Corporation* may be tempted to argue that the words "strict compliance" are essential before its jurisprudence is applied. Parties seeking to rely on *Maeda Corporation* may be tempted to argue that the strict adherence to 'time-bar' comes from plain wording of such clauses such that there is no need to look at the commercial purpose.[3]

The 'Time-Bar' Clause

Put simply, the JV Plaintiffs (Maeda Corporation and China State Construction Engineering) were the main contractors under the Main Contracts with the Mass Transit Railway Corporation (MTRC or the "Employer") for the construction of tunnels for the Hong Kong to Guangzhou Express Rail Link. The plaintiffs subcontracted the diaphragm wall works to the defendant sub-contractor, Bauer. Disputes arose which were submitted to arbitration initiated by the defendant, and this led to various interim awards. Bauer's primary case in the arbitration was that the unforeseen ground conditions gave rise to a variation of the scope of works under the sub-contract, so as to entitle Bauer to claim additional payment under the express variation provisions. In the alternative, Bauer made a "like rights" or 'equivalent relief' claim under sub-clause 1 of Clause 21.1 of the sub-contract. The arbitrator rejected the variation claim on the basis that where in carrying out the diaphragm wall work Bauer encountered unanticipated ground conditions, it was still obliged to carry out the same work in terms of the volume of material that had to be excavated and there was no change to the scope of the work. Nor was there any instruction issued by the engineer and/or by the JV. Therefore, the question whether the "like rights" claim had been notified to the JV pursuant to the relevant 'time-bar' clause became the battleground.

Clause 21 of the sub-contract stated:

> 21.1 If the Sub-Contractor intends to claim any additional payment or loss and expense pursuant due to:
>
> 21.1.1 **any circumstances or occurrence as a consequence of which the Contractor is entitled to additional payment or loss and expense under the Main Contract;**
>
> 21.1.2 any alleged breach of the Sub-Contract, delay or prevention by the Contractor or by his representatives, employees or other sub-contractors;
>
> 21.1.3 any claim for discrepancy between Sub-Contract Drawings and documents pursuant to Clause 8.4;
>
> 21.1.4 any claim under Common Law, statute laws or by-law;

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21.1.5 any extension of time granted to the Sub-Contractor with exception to those cases which the delay are caused by typhoon signal no. 8 and/or force majeure etc.

21.1.6 any Variation of Sub-Contract Variation,

as a condition precedent to the Sub-Contractor's entitlement to any such claim, the Sub-Contractor shall give notice of its intention to the Contractor within fourteen (14) days after the event, occurrence or matter giving rise to the claim because apparent or ought reasonably to have become apparent to the Sub-Contractor. For the avoidance of doubt, the Sub-Contractor shall have no entitlement to any additional payment or any additional loss and expense and no right to make any claim whatsoever for any amount in excess of the Sub-Contractor Sum in respect of any event, occurrence or matter whatsoever unless this sub-Contractor sets out an express right to that additional payment, additional loss and expense or claim.

21.2 If the Sub-Contractor wishes to maintain its right to pursue a claim for additional payment or loss and expense under Clause 21.1, **the Sub-Contractor shall as a condition precedent to any entitlement, within twenty eight (28) Days after giving of notice under Clause 21.1, submit in writing to the Contractor:**

21.2.1 **the contractual basis** together with full and detailed particulars and the evaluation of the claim;

21.2.2 where an event, occurrence or matter has a continuing effect or where the Sub-Contractor is unable to determine whether the effect of an event, occurrence or matter will be continuing, such that it is not practicable for the Sub-Contractor to submit full and detailed particulars and the evaluation in accordance with Clause 21.2.1, a statement to that effect with reasons together with interim written particulars. The Sub-Contractor shall thereafter, as a condition precedent to any entitlement submit to the Contractor at intervals of not more than twenty eight (28) Days (or at intervals necessary for the Contractor to comply with his obligations under the Main Contract, whichever is shorter) further interim written particulars until the full and detailed particulars are ascertainable, whereupon the Sub-Contractor shall as soon as practicable but in any event within twenty eight (28) Days (or as necessary for the Contractor to comply with his obligations under the Main Contract, whichever is shorter) submit to the Contractor full and detailed particulars and the evaluation of the claim;

21.2.3 details of the documents and any contemporary records that will be maintained to support such claim; and

21.2.4 details of the measures which the Sub-Contractor has adopted and proposes to adopt to avoid or reduce the effects of such event, occurrence or matter which gives rise to the claim.

21.3 **The Sub-Contractor shall have no right to any additional or extra payment, loss and expense, any claim for an extension of time or any claim for damages under any Clause of the Sub-Contract or at common law unless Clauses 21.1 and 21.2 have been strictly complied with.** [emphasis added]

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The condition precedent Clause 21.2.1 required Bauer to specify the contractual basis of its claim. Clause 21.3 stated that Bauer would have no entitlement to additional time and/or money unless Clause 21.2 had "been strictly complied with." The "like rights" claim is set out in Clause 21.1.1, but had it been notified pursuant to Clause 21.2.1?

The Arbitrator's Approach

Bauer's Clause 21.2 notice did not make express reference to a claim under Clause 21.2.1. There was no dispute about that specific point. The arbitrator found that the appropriate Clause 21.2 notice had nevertheless been given (despite the fact that Bauer had made its claims based on a variation or sub-contract variation (under Clause 21.1.6), and not on a "like rights" basis under Clause 21.1.1). The arbitrator made it clear in the award that the claim allowed in the arbitration is a new legal basis, but that Bauer was not precluded under Clause 21.2 to pursue a different contractual or legal basis. The Arbitrator stated:

> "I consider that both as a matter of sympathy and as a matter of construction, the contractual basis of the claim stated in the Clause 21.2 notice does not have to be the contractual basis on which the party in the end succeeds in an arbitration. First, to expect a party to finalize its legal case within the relatively short period and be tied to that case through to the end of an arbitration is unrealistic. Secondly, what is important from the point of view of the [JV] is to know the factual basis for the claim so that it can assess it and decide what to do.
>
> Indeed, as can be seen on the facts here, the JV's view of the appropriate legal basis for the claim was that it was a Clause 38 unforeseen physical conditions claim as well as a Variation claim, as shown in the notices which were then given to the MTRC. It therefore follows that the fact that Bauer have made its claims on the basis of the relevant claim being a Variation or Sub-Contract Variation does not preclude Bauer from making the claim on a new legal basis based on notices given by reference to a different legal basis."

The Courts' Approach

Both the Court at First Instance and the Court of Appeal of Hong Kong disagreed with the arbitrator. The Court at First Instance made clear that the claim pursued by Bauer in the arbitration, and the subject matter of the Award, is a claim for additional payment or loss and expense pursuant to "any circumstances or occurrence as a consequence of which the Contractor is entitled to additional payment or loss and expense under the Main Contract," under Clause 21.1.1 but that specific claim had not been isolated in the notice issued under Clause 21.2. This omission was fatal because "Clause 21.3 clearly states that the Defendant 'shall have no right' to any additional or extra payment, loss and expense, under any Clause of the Sub-Contract or at common law 'unless Clauses 21.1 and 21.2 have been strictly complied with.'"[4] The learned Judge stated:

> [23] In my view, there can be no dispute, and no ambiguity, from the plain and clear language used in Clause 21, that the service of notices of claim in writing referred to in Clause 21.1 and 21.2 are conditions precedent, must be "strictly" complied with, and failure to comply with these conditions will have the effect that the Defendant will have "no entitlement" and "no right" to any additional or extra payment, loss and expense.

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The arbitrator had considered that the principal purpose of Clause 21 was to enable the JV to know the factual basis for the claim so that it can assess it and decide what to do and that purpose had been complied with because the JV had made a unforeseen physical conditions claim upstream to the Employer. The Court at First Instance disagreed, stating[5]:

> "There is commercial sense in allocating risks and attaining finality by designating strict time limits for claims to be made and for the contractual basis of claims to be specified. In particular, the language used in Clause 21.1 is in my view clear on its plain reading, and the decisions in *Rainy Sky SA v Kookmin Bank* [2011] UKSC 50 and *Arnold v Britton* [2015] AC 1619 highlight the importance of the language used in the provision to be construed, notwithstanding the need to read such language in the proper factual and commercial context. There is no basis for a court or tribunal to rewrite the Sub-Contract or Clause 21 for the parties after the event."

Put shortly, the Hong Kong Court of Appeal endorsed the first instance judge's jurisprudence. The Court of Appeal considered whether on the proper interpretation of Clause 21, Bauer was precluded from amending or substituting the stated contractual basis by making its claim in arbitration on a different contractual basis outside the 28 days of the relevant notice given under Clause 21.1. Having decided, "[t]he wording of Clause 21.2.1 is clear and unambiguous. Within the stipulated time, the Sub-Contractor is required to give notice of the contractual basis, not any possible contractual basis which may turn out not to be the correct basis," the Court of Appeal supplemented the analysis by making it clear that Bauer is precluded from changing the contractual basis of its claim and stated "[t]he arbitrator's interpretation of Clause 21.2.1 would negate the commercial purpose of achieving finality, as a claim can be advanced on a different contractual basis in an arbitration which may be years down the line." The Court of Appeal went even further by explaining that the second commercial purpose for Clause 21.2.1 was that, in a chain contract situation, the JV would wish to know whether the sub-contractor's claim would need to be passed up the line to the Employer.[6] If the claim is based on other matters, such as breach of the sub-contract by the JV (Clause 21.1.2), it would not need to be. Put simply, the Court of Appeal rejected the arbitrator's interpretation stating that it "may prejudicially affect this commercial purpose as well."[7]

[1] *Maeda Kensetsu Kogyo Kabushiki Kaisha also known as Maeda Corporation and Another v. Bauer Hong Kong Ltd* [2020] HKCA 830; CACV 301/2019 (16 October 2020).

[2] Clause 20.2.4 of the Second Edition of the FIDIC Silver Book requires the claiming party to submit a "fully detailed claim" which includes "a statement of the contractual and/or other legal basis of the Claim" within either "84 days after the claiming Party became aware, or should have become aware, of the event or circumstance giving rise to the claim, or such other period (if any) as may be proposed by the claiming Party and agreed by the other Party."

[3] In *Teesside Gas Transportation Limited v. (1) Cats North Sea Limited* [2020] EWCA Civ 503 Males LJ said at [55]

> 'The court's approach to the construction of commercial contracts is now well known and was not in dispute. Absent further intervention by the Supreme Court, the principles can now be taken as settled. They have been re-stated in *Arnold v Britton* [2015] UKSC 36, [2015] AC 1619 and *Wood v Capita Insurance Services Ltd* [2017] UKSC 24, [2017] AC 1173 and need not be repeated here.'

Males LJ continued at paragraph 56 by reference to the five factors in *Arnold v Britton*: "I propose to undertake the 'unitary exercise' of construction by considering (1) the language of [the clause], (2) other relevant provisions of the Agreement, (3) the overall structure of the Agreement's payment provisions, (4) the background circumstances known to the parties at the time the Agreement was concluded, and (5) commercial common sense."

[4] *Maeda Kensetsu Kogyo Kabushiki Kaisha also known as Maeda Corporation and Another v. Bauer Hong Kong Ltd* [2019] HKCFI 916; HCCT 4/2018 (9 April 2019) at Paras 20–23.

[5] *Maeda Kensetsu Kogyo Kabushiki Kaisha also known as Maeda Corporation and Another v. Bauer Hong Kong Ltd* [2019] HKCFI 916; HCCT 4/2018 (9 April 2019) at Para 31.

[6] Clause 38.1 of the main contract provided, inter alia: "If however during the Execution of the Works the Contractor shall encounter within the Site physical conditions (other than weather conditions or conditions due to weather conditions) or artificial obstructions which conditions or obstructions he considers could not reasonably have been foreseen by an experienced contractor at the date of the Letter of Clarification, and the Contractor is of the opinion that additional Cost will be incurred which would not have been incurred if the physical conditions or artificial obstructions had not been so encountered, he shall if he intends to make any claim for additional payment comply with Clause 82 …" It was accepted by the JV that in principle and subject to complying with the notice provisions in Clause 21, pursuant to Clause 21.1.1 Bauer would have a "like rights" claim and be entitled to be paid a proportion of any amount paid under the main contract for a Clause 38 claim.

[7] *Maeda Kensetsu Kogyo Kabushiki Kaisha also known as Maeda Corporation and Another v. Bauer Hong Kong Ltd* [2020] HKCA 830; CACV 301/2019 (16 October 2020) at Para 61.

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