Global projects & construction

infrastructure insights

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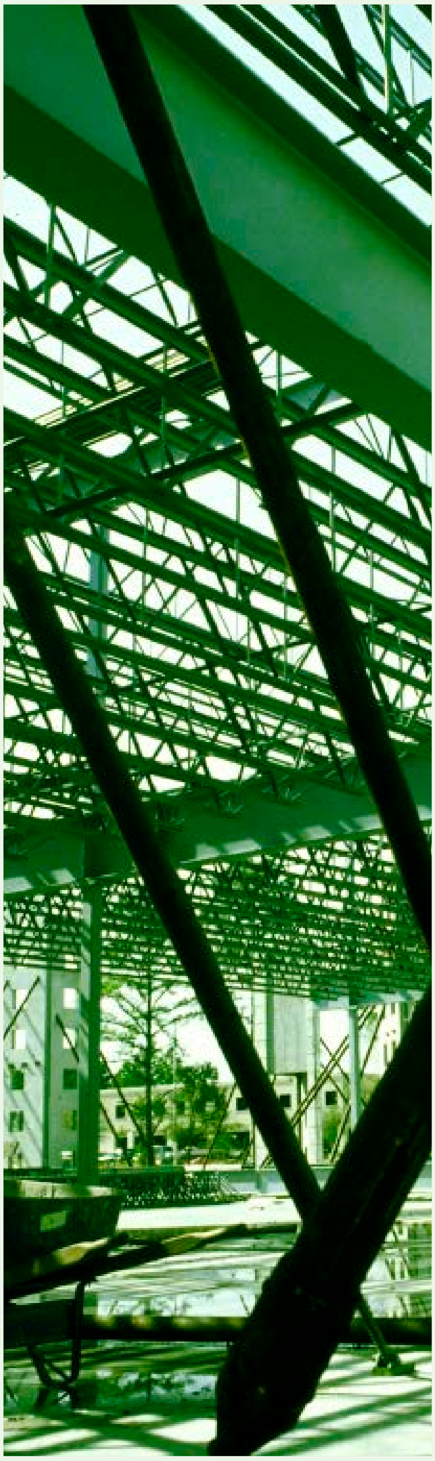

Introduction

Welcome to the inaugural edition of our **Infrastructure Insights** newsletter which reviews a wide range of issues impacting the global infrastructure sector.

This edition provides insights on:

We hope you find **Infrastructure Insights** an informative and useful read.

Should you have feedback or suggestions for future topics, please contact **infrastructure@clydeco.com**. Similarly, to hear more from our global projects & construction group, email us providing your area(s) and region(s) of interest.

Pay up or pay out: a warning to head contractors

By Beth Cubitt and Paul Morgan

In the last two years, more than 1,000 construction companies have entered into external administration in New South Wales. The effects and impact of insolvency in the construction industry are not just restricted to the failed company. The effects are felt by many parties, especially those further down the contract chain, who may be ill-equipped to deal with persistent delays in cash flow.

The findings of the Inquiry into Construction Insolvency noted an industry-wide concern with a number of key problems:

- Subcontractor payment cycles are unacceptably long
- Delayed/reduced payments to sub-contractors increase financial pressure down the contracting chain
- The resulting financial stress on subcontractors leaves them in significant risk of insolvency

Against that backdrop, the NSW Government proposed to change the law and has drafted a bill* to make changes to the Security of Payment Act 1999 (NSW).

Key changes will include provision that:

- Principals will be required to pay Head Contractors no later than 15 days after a payment claim is submitted to a Principal
- Head Contractors will be required to pay Subcontractors (and likewise Subcontractors to pay Suppliers) no later than 30 days after a payment claim is submitted to a Head Contractor (or to a Subcontractor in the case of a payment claim from a Supplier)
- Where the works are in respect of a residential property where the principal resides at the property, payment to Subcontractors or Suppliers must be by the contractually agreed date, or if none is specified, by no later than 10 days after the payment claim is submitted

The Bill provides that parties to any applicable contract will be free to agree shorter timeframes, but not longer timeframes.

The payment requirements will not apply to principals where the principal resides at the property where the works are taking place.

In addition, Head Contractors should be aware that penalties will be introduced in order to ensure transparency in the payment practices operating in the industry and to incentivise Head Contractors to pay.

If a Head Contractor:

- fails to supply a supporting statement with their payment claim to a principal that includes a declaration that all subcontractors and suppliers (if any) have been paid in full
- supplies a statement that is false or misleading; then they will face a maximum fine of AUD 22,000 or three months imprisonment or both

In order to preserve compliance with these amendments, the Bill will also give power to authorised public service employees to make written requests that a Head Contractor provide information and all documents related to the payment of subcontractors.

Failure of a Head Contractor to comply with these requests will also incur a maximum fine of AUD 22,000 or three months imprisonment or both.

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* Since this article was first published, the relevant amendments have come into force, applying to contracts entered into from 21 April 2014

Private airport management in Indonesia: tenders expected in 2014

By Michael Horn

Last year, Indonesia announced it would offer regional airport management contracts to the private sector under a public-private partnership (PPP) scheme, beginning with 10 existing airports. Taking the next step in realizing this new policy, the Indonesian Ministry of Transportation recently announced that tenders for the management of three airports – located in Lampung, Komodo and Palu, Sulawesi - will commence in August/September 2014.

This announcement hints at the potential for big changes in the Indonesian airport sector. The sector has long been dominated by the state through public ownership and management by the Ministry of Transportation and state-owned operators Angkasa Pura I and Angkasa Pura II. Indonesia is now looking to airport management by the private sector to address the twin challenges of rising demand on airports, many operating beyond design capacity, and anticipated growth fueled by open access mandated from 2015 by the ASEAN Open Skies Policy.

It is hoped private airport management will also deliver budget savings, freeing funds to develop other airports. "Pioneer" airports in remote areas have been cited as the intended beneficiaries of increased state investment out of reallocated funds.

Local news sources report 38 investors (13 local and 25 foreign) have already expressed interest in the 10 airport management PPPs. The local investors are said to include Garuda Indonesia, Lion Air and the Bakrie Group. The foreign investors' names have not been formally disclosed, but appear to reflect broad global interest. They are rumored to include 13 investors from Japan, three from Singapore, two from Spain, two from Australia and one from each of New Zealand, Malaysia, United Arab Emirates and South Korea. One multilateral lending institution may also throw its hat in the ring.

Foreigners may soon be in the hunt for local partners, as regulations limit airport management to Indonesian companies with no more than 49% foreign ownership.

In addition to airport management opportunities, the private sector may soon be offered a role in airport ownership and development. The Ministry of Transportation is planning to offer several new airport PPP projects. These new airports may include Karawang International Airport near Jakarta, Kulonprogo Airport in Yogyakarta, Kertajati Airport in West Java and Buleleng Airport in North Bali. As of May 2014 these projects are still in the preparation stage. Clyde & Co will soon publish analysis of the Karawang International Airport and Kertajati Airport projects.

We set out a summary of the 10 airports proposed for the PPP management scheme, as follows:

Airport	Location and status	Information
Radin Inten II Lampung Selatan Airport	– Bandar Lampung, Lampung Province, – Domestic airport, domestic routes	– Recently renovated – Currently managed by the Department of Transportation – Annual passengers of up to 1 million – Garuda Indonesia, Lion Air and Sriwijaya Air currently service – Single 2,500m runway – Local government has set aside Rp. 2 billion (approximately USD 173,684) to further renovate the airport and extend the runway to 3,000m – Local government has expressed its intention to introduce international service

Airport	Location and status	Information
Komodo Airport	– Near Labuan Bajo, Flores Island, East Nusa Tenggara Province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Annual passengers of up to 800,000 – Airlines currently operating include Garuda Indonesia, Sky Aviation, Transnusa and Wings Air – Single 2,150m runway – Garuda Indonesia has filed an expression of interest to manage the airport due to its tourism potential. Labuan Bajo is the departure point for tours to Komodo National Park, home of Komodo dragons – The airport has been undergoing an expansion process since 2013. Progress, however, has been slow
Mutiara Sis Aljufri Airport	– City of Palu in Central Sulawesi – Domestic airport, domestic routes	– Formerly named Mutiara Airport. The name change is effective as of March 2014 following the construction of a new terminal building – Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Annual passengers of up to 800,000 – Airlines currently operating include Garuda Indonesia, Lion Air and Sriwijaya Air – Single 2,390m runway – The local government plans to extend the current runway to 2,500m by 2015
Fatmawati Soekarno Airport	– Bengkulu City, Bengkulu Province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Annual passengers of up to 670,000 (as of 2012) – Airlines currently operating include Garuda Indonesia, Lion Air, Sriwijaya Air and Susi Air – Single 2,250m runway – In January 2014 the local government announced its plans to (i) build a new airport in Padang Pelawi Regency since it is no longer possible to carry out airport expansion in the current location and (ii) develop international services at the new airport
Sentani Airport	– Jayapura, Papua Province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Airlines currently operating include Garuda Indonesia, Lion Air, Sriwijaya Air, Express Air and Batik Air – Single 3,000m runway – The airport was expanded in early 2014. A new terminal may also be built to accommodate increasing passengers numbers
Matahora Airport	– Wangi-Wangi Island, Wakatobi Regency, Southeast Sulawesi Province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – May be one of the most sought after airports due to the tourism potential in Wakatobi. Garuda Indonesia has expressed its interest in managing the airport – Airlines currently operating include Garuda Indonesia, Susi Air, Express Air and Wings Air – Single 2,121m runway – As of March 2014, the local government has requested funds from the Ministry of Transportation to expand the airport. The expansion project is expected to be completed in early 2015

Airport	Location and status	Information
Tjilik Riwut Airport	– City of Palangkaraya, Central Kalimantan Province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Airlines currently operating include Garuda Indonesia, Lion Air, Citylink and Aviastar – Single 2,600m runway – In January 2014, the local government announced its plan to relocate to a new airport at Hampalit Village since the current airport can no longer be expanded
H.A.S Hanandjoeddin Airport	– Tanjung Pandan, Belitung Regency, Bangka Belitung Province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Airlines currently operating include Garuda Indonesia, Citylink, Sriwijaya Air, Wings Air and Sky Aviation – Single 2,250m runway – The airport is attractive to investors due to the tourism potential in Bangka and Belitung Islands – In December 2013, the local government announced its plan to expand the airport and introduce international services by 2015
Juwata International Airport	– Located in Tarakan, North Kalimantan Province – International airport, domestic and international routes (to Tawau and Kota Kinabalu in Malaysia)	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Airlines currently operating include Garuda Indonesia, Kalstar Aviation, MASwings, Lion Air, MA Indonesia, Sriwijaya Air and Susi Air – Single 2,500m runway – In April 2014, the local government announced plans to build a port near the Juwata airport to provide faster transfer to neighbouring islands (including the increasingly popular Derawan Island)
Sultan Babullah Airport	– Ternate, North Maluku province – Domestic airport, domestic routes	– Currently managed by the Technical Management Unit of the Directorate General of Air Transportation – Airlines currently operating include Garuda Indonesia, Lion Air, Express Air and Sriwijaya Air – Single 2,350m runway – In September 2013, the airport launched a new terminal to accommodate increasing passenger numbers

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Institutional investors and the infrastructure investment paradox

By Judith Donnelly and Corina Barsa

The central paradox facing the infrastructure industry today is that while some 60% of institutional investors have underspent their allocations to infrastructure, there is a global shortfall of investment in infrastructure of over USD 1 trillion per year.

The gap can be bridged by improving communication between stakeholders structuring investment opportunities with the needs of institutional investors in mind. This article examines what those needs are.

A match made in heaven?

Institutional capital is increasingly taking the place of bank lending, as banks deleverage and the low-return investment environment forces institutional investors to diversify their portfolios. The UK Chancellor, George Osborne, has set the Government the ambitious target of securing GBP 200 billion of institutional capital for investment in UK infrastructure projects.

At first glance, infrastructure appears to be an ideal asset class for institutional investors. Pension funds and insurance companies, with long-term liabilities and exposure to inflation risk, are attracted to the stable, inflation-linked cash-flows of infrastructure. Sovereign funds who need to deploy large amounts of capital over a long-term horizon are also often attracted to the potential returns from the asset class.

Yet there has been some frustration with the slow rate of progress in accessing capital from these institutional investors for investment in infrastructure. Better communication between investors and those seeking their capital, as well as creative structuring of investment opportunities, is needed in order to bring the two sides of the equation together.

Portfolio construction

Anyone seeking to attract institutional capital needs firstly to understand how infrastructure fits into the overall portfolio of an institutional investor. As a recent report from the World Economic Forum highlights:

> Investors evaluate an infrastructure opportunity in relation to other asset classes such as government bonds, equity markets and private equity. That is to say, investors evaluate not just how but whether to invest in infrastructure at all.[1]

People seeking investment need to understand that not only are they competing for capital with other infrastructure projects in their country, but they are competing against other asset classes and across global markets.

Institutional investors are generally conservative and invest predominantly in gilts, corporate bonds and listed equities. It is normal for such an investor to have no more than 25% of their portfolio invested in what they term 'alternative' asset classes, which encompasses a broad range of assets from hedge funds to private equity and infrastructure.

Allocations to 'alternatives' have increased over the past ten years due to low gilt yields and a low-return investment environment. However, infrastructure is still fairly novel to the institutional investment community and is often considered more cutting-edge than asset classes which may on their face appear riskier, such as hedge funds.

Who's afraid of construction risk?

There is an urban myth that institutional investors will not invest in greenfield projects as they are deterred by construction risk, but this is not always the case. Many pension funds and other institutional investors are aware that in order to secure higher returns from their infrastructure assets, they need to take some of the construction risk.

More importantly, the 'holy grail' for pension funds is inflation linkage (since their liabilities are inflation linked) and with most secondary market assets, this has been stripped out. Pension funds are increasingly aware that in order to secure inflation linkage, they need to structure the assets themselves, which means involvement in the construction phase.

On the other hand, institutional investors can be reluctant to invest in projects with significant demand risk, hence the preference for taxpayer-funded social infrastructure projects. To secure more funding for UK infrastructure projects, the UK Government should consider ways of managing demand risk. There have been many creative solutions proposed, such as franchising regions of road networks rather than seeking investment in a toll road.

One size does not fit all

It should also be borne in mind that pension funds, sovereign funds and insurance companies have slightly different needs and risk tolerances. Pension funds have to comply with statutory guidelines on risk and diversification, and insurance companies have regulatory capital requirements.

Sovereign funds, which do not have fixed liabilities and have the longest term horizons, are more likely to seek the high returns from economic infrastructure projects such as HS2 or investment in nuclear power. Some pension funds prefer the low-risk, predictable cash-flows from social infrastructure and renewables.

Targeting the right institution and creating an investment portfolio which fits the requirements of the targeted investor will be key in securing financing for infrastructure projects.

It's good to talk

Greater dialogue between the Government and institutional investors can ensure that investment opportunities are packaged in a way that is attractive and comprehensible. Clyde & Co have been working closely over the past several years with a range of institutional investors and academic institutions across the world, including the seed investors in the Pensions Infrastructure Platform, and are well-placed to advise on the opportunities in this market.

We are optimistic that the gap can be bridged, and that the billions of pounds of capital looking for a home can be used to provide the investment in global infrastructure that is critically needed.

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[1] Infrastructure Investment Policy Blueprint, World Economic Forum, February 2014

Public private partnerships in Tanzania: update following the Finance Act 2013

By Peter Kasanda

Following a briefing issued in September 2013 focusing on Public Private Partnerships (PPP) in Tanzania, you will recall that there are two types of PPP Project, namely solicited and unsolicited.

Both solicited and unsolicited proposals are governed by the Public Private Partnership Act 2010 (the **PPP Act**) and the Public Procurement Act 2011. A solicited proposal is one initiated by the public sector. By contrast, an unsolicited proposal is one initiated by the private sector.

Crucially, both types of PPP had to be competitively tendered at a specific point in the project cycle. The only difference being that, Section 80(1) of the Procurement Act 2011 allowed for an '*advantage*' to be given to the unsolicited proposal during the tender process in recognition of the time and expense involved in generating the proposal. The legislation did not prescribe the form of advantage.

Following the implementation of the Finance Act 2013 (the **FA 2013**), unsolicited proposals no longer need to be competitively tendered. Sections 40 and 43 of FA 2013 amend the PPP Act and the Public Procurement Act 2011 respectively.

Unsolicited proposals are defined under the Public Private Partnership Regulations 2010 (the **PPP Regulations**) as "*written proposals that are submitted to a relevant contracting authority on the initiative of the private party for the purpose of entering into a public private partnership agreement with the government*".

Previously after conducting a feasibility study, a Contracting Authority (**CA**) (who is any ministry, government department, local government authority or statutory corporation) would invite tenders from interested private entities to bid for a project.

The current position with regards to unsolicited proposals stipulates that a party submitting an unsolicited proposal shall not be subject to a competitive bidding process.

Thus after the approval of the project agreement by the minister responsible, the procuring entity will submit an application together with other supporting documents for the Public Procurement Co-ordination Unit (**PPCU**) Assessment and approval. (Rule 21 of the PPP Regulations).

The below flowchart summarises phases of the PPP project cycle in relation to solicited and unsolicited proposals in light of the FA 2013 provisions:

Solicited bid: phases of the PPP project cycle

Initial project selection
Minister responsible for investment establishes a list of potential PPP projects.

Pre-feasibility study
CA undertakes pre-feasibility study.

Feasibility study
CA undertakes or orders feasibility study.

Final approval
CA submits project to minister responsible for the CA/PPPCU/PPPFU and the minister responsible for finance for approval/ rejection of the projects.

Procurement and contract award
CA conducts procurement process and signs contract.

Implementation
CA performs contract management for the duration of the contract.

Unsolicited bid: phases of the PPP project cycle

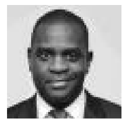
Project concept
Private party submits a project concept to the CA. CA has 21 days to accept or reject project concept.

Feasibility study
Private party carries out a feasibility study.

Approval of project agreement
CA submits draft project agreement to Minister responsible for the CA/PPCU/ PPFU/Minister responsible for Finance for approval/rejection and to Attorney General who provides legal opinion.

Project agreement
CA alters project agreement in line with Attorney General's legal opinion and signs agreement (CA can terminate agreement at any time).

Implementation
CA performs contract management for the duration of the contract.



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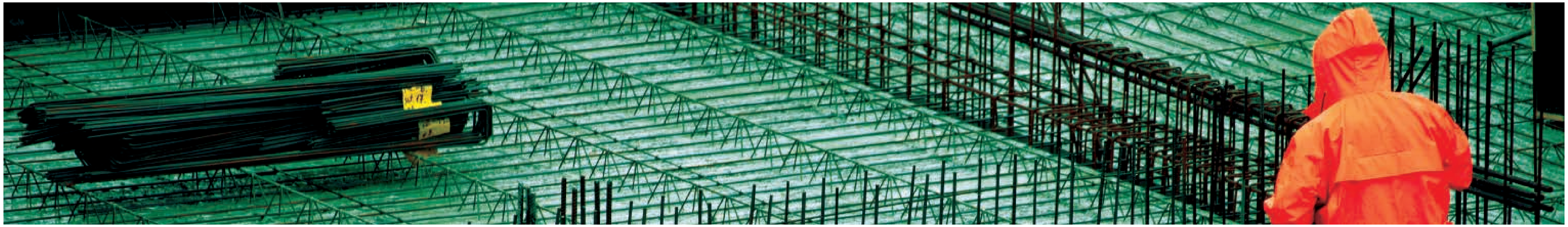

Terminating a FIDIC Contract: what's in a notice?

By Tia Starey

Notices serve many important functions on construction projects. They are the means by which employers (usually acting through a contract administrator) issue instructions for matters such as variations, and the way contractors are able to claim for extensions of time and additional cost. They are also, crucially, the means by which either party may seek to terminate the contract. As part of the termination process, the question as to whether or not a notice has to strictly comply with contractual requirements is an important one.

A recent case in the Technology and Construction Court (TCC) in England has shed some light on this question in the context of the 1999 FIDIC Yellow Book, with potentially some quite welcoming results for those looking to terminate.

FIDIC provisions

The major FIDIC forms of contract (the 1999 Red, Yellow and Silver Books) contain almost identical provisions on notices. Clause 1.3 sets out that all notices must be in writing and delivered by hand (against receipt), or sent by mail, courier or by e-mail (if email is specified in the contract). The notice must be sent to the address specified in the contract, unless either the recipient gives notice of another address or sends a request for approval or consent from a new address (this might occur, for example, if the contractor sends a request from a different email address). Clause 15 deals with termination by the Employer. This provision allows the Employer to terminate for contractor default, insolvency and for convenience. Where Contractor default is alleged, the Employer is required to first issue a "notice to correct" prior to issuing a notice of termination.

The case

In *Obrascon Huarte Lain SA v Her Majesty's Attorney General for Gibraltar* [2014] EWHC 1028 (TCC), the Employer did not comply with all the requirements of clause 1.3 when issuing the clause 15 correction notice and the termination notice to the Contractor, Obrascon Huarte Lain SA ("OHL").

Instead of issuing these notices to the address specified in the Contract, which was OHL's head office in Madrid, it issued the notices to the site office in Gibraltar. It subsequently re-served the notices, but the Contractor argued that the initial failure to comply amounted to a repudiation of the contract by the Employer.

The Employer, the Government of Gibraltar, had engaged OHL, a Spanish civil engineering contractor, under a substantially un-amended FIDIC Yellow Book to design and construct a road and tunnel near and under the Gibraltar Airport runway. The project encountered severe delays, mainly as a result of contaminated ground conditions, which the Contractor unsuccessfully argued were due to unforeseeable adverse physical conditions. The project was meant to be completed within two years, but after two and a half years, only 25% had been completed. The Government of Gibraltar took the view that these delays constituted a failure by OHL to carry out its obligations under the contract, and thus was a ground for termination.

The judgment, in addition to providing fresh guidance on the concept of "unforeseeable adverse physical conditions", provides a useful interpretation of the notice provisions under the FIDIC forms of contract, particularly in the context of termination. One of the questions before the court was whether the notice had been effective or not, or in other words, was the failure to comply fully with clause 1.3 fatal to the termination?

Substantive compliance

The Judge, Mr Justice Akenhead, reviewed a string of cases which had looked at the question as to whether "strict compliance" was necessary to make a notice effective. The wording of the clause was vital: did it expressly set out that the notice needed to comply with clause 1.3 to be valid? The answer was no: under the FIDIC Yellow Book, clause 15 and clause 1.3 do not contain words that make strict compliance a "condition precedent" to termination. The Judge was keen to stress that in answering this question in the context of building and engineering contracts, commercial realities need to be taken into account, including what was the "primary purpose" of the clause. If the purpose could be achieved without strict compliance, as was the case here, then strict compliance was not necessary.

However, the Judge was also keen to stress that termination was a "serious step" and that there "needs to be substantive compliance with the contractual provisions to achieve an effective contractual termination". This required the notice to be given in sufficiently clear terms, and served on a person with appropriate seniority within the company. In this case, the notice had been served on OHL's Project Manager at the site office where many other communications had been sent and received, and therefore this requirement was satisfied.

No repudiation

Having decided that the notice had been validly served, Mr Justice Akenhead did not need to deal with the issue of repudiation. However, he took the opportunity to observe that the technical deficiencies in the notice would not amount to a repudiation of the contract by the Employer. Relying on past authorities, he held that the service of a "valid and actually well-founded termination notice at the technically wrong address" could not constitute a repudiation of the contract. It was therefore the Contractor who had repudiated the contract and not the Employer, when erroneously treating the contract as being at end on the grounds of ineffective service. Further, the Judge noted that the subsequent issue of a conforming notice would in any event have "cured" the initial deficiencies.

Conclusion

This judgment provides some comfort to those wishing to terminate: it is clear that under the FIDIC forms of contract a "commercially realistic interpretation" needs to be taken, and that strict compliance is not necessary in order for a termination notice to be effective. That said, in all cases it will be necessary to show that the notice has actually been served, and the easiest way to do this of course will be to comply with the contractual provisions

In short, many of these issues can be avoided. Time invested at the outset of a project in thoroughly drafting or reviewing the terms of a contract and getting it right is time well spent. Adopting even simple measures will go a long way.

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Saudi Arbitration Law 2012: the positive impact projected?

By Ben Cowling

In April 2012, the Kingdom of Saudi Arabia (KSA) enacted a new Arbitration Law which was hailed as a boon for investors and a major step forward for commerce. Two years on, we consider whether the law is having the positive impact anticipated.

As the largest economy in the Arabian Gulf, KSA offers a wealth of potential for both domestic and international companies seeking to do business in the Kingdom. Yet its legal system remains a somewhat uninviting jurisdiction for foreign investors: its substantive law is based on Shari'ah, and the absence of a system of binding precedent means local courts are bestowed with broad discretion to determine disputes. Unsurprisingly, foreign investors seek to mitigate risk by including arbitration clauses when contracting with Saudi parties. Arbitration, however, is not a panacea for any given problem a party may encounter when seeking to resolve a dispute in the Kingdom.

The construction landscape

The KSA construction market is very strong, with an estimated USD 600 billion in construction projects planned or underway[2]. Projects such as the USD 22.5 billion Riyadh Metro Project (the world's largest) have attracted foreign construction companies and consultants from a diverse range of countries, including Spain, Italy, Germany, India, Korea, Canada, the USA and the UK. Other current landmark projects are King Abdullah Financial District, the Riyadh Airport redevelopment and the Haramain High Speed Rail project. Having taken on obligations to deliver projects of this scale, foreign companies need to actively manage many large legal and commercial risks and we commonly see arbitration clauses in main contracts (subject to the restrictions in the government tenders law), subcontracts, joint venture arrangements and consultancy appointments.

Revised legislation

In theory, the 2012 Arbitration Law significantly improved the legal landscape for arbitration in KSA, which had previously been governed by an Arbitration Law enacted in 1983. In the intervening years, the Kingdom acceded to the New York Convention (1994) and the United National Commission on International Trade Law (UNCITRAL) created the 'Model Law on International Commercial Arbitration' (1985, with amendments in 2006). The 2012 Arbitration Law is based on the Model Law but incorporates significant local law elements; for example, any arbitral award can be challenged if it is inconsistent with Shari'ah. The Law applies to both domestic arbitration and international commercial arbitration with a Saudi seat, but not to foreign arbitral awards; with its remit limited in this way, the new law only went so far in ameliorating the legal environment for parties arbitrating disputes in the Kingdom.

Positive outcomes

Even so, a number of positive trends have materialised as a result of the new legislation: the local courts have been generally supportive, for example in a number of cases they have declined to hear claims subject to binding arbitration clauses; and courts have recognised parties' rights under the 2012 Law to adopt the rules of external arbitration centres as their agreed procedures. Indeed, in a recent case concerning an arbitration governed by the International Chamber of Commerce (ICC) Rules, the Dammam Court of Appeal required the claimant to file its Request for Arbitration with the ICC as the first step, and therefore declined the claimant's application for the court to appoint the arbitrators.

Furthermore, arbitral awards (domestic and foreign awards with Saudi seats) made under the 2012 Law have the same status as court decisions once they are ratified; and, combined with the 2013 Enforcement Law, there is now a detailed process available to parties for converting an arbitral award into a recovery.

This recent Enforcement Law also provides true benefit to parties attempting to enforce foreign awards in KSA. For a foreign award to be successfully enforced, it has long been a requirement that the award be both consistent with Shari'ah and made in a location that reciprocally enforces Saudi judgements and awards.

The benefit of the 2013 Enforcement Law is that the reciprocity requirement can be satisfied by the Ministry of Justice releasing an official statement that the issuing jurisdiction is on the approved list, if applicable. This obviates the need for courts to decide whether the seat of the arbitration is "reciprocal" and is a great step forward in overcoming practical obstacles to the recognition and enforcement of foreign arbitral awards in Saudi Arabia.

Room for improvement

Whilst elements of the legal framework necessary for arbitration have been put in place, significant drawbacks to arbitrating disputes remain. For example, courts still display a tendency to intervene in arbitration cases, contrary to the 2012 Law: in a recent case under UNCITRAL Arbitration Rules, the Dammam Court of Appeal has required the parties to nominate their arbitrators at scheduled court hearings, rather than allowing them to follow the procedure for appointing arbitrators under the Rules.

There is also a degree of uncertainty surrounding how the 2012 Law should be applied, given that Implementing Regulations (common with Saudi legislation) have yet to be passed in relation to the 2012 Law. For example, at present, it is not clear whether a sole arbitrator or a tribunal chairman must be a Saudi national, or a foreign Muslim, as per the requirements under the 1983 Law. The 2012 Law states only that a sole arbitrator or chairman must be 'of full capacity, of good conduct and reputation and the holder of at least a university degree in legal science'. Accordingly, it is unclear whether an arbitral award made on the basis of the 2012 Law could be challenged if the sole arbitrator or chairman was not a Saudi national or a Muslim foreigner. Prompt enactment of the Implementing Regulations would resolve this issue, and others, before they develop.

Demonstrable commitment

Another development which should serve to improve the situation is the recent announcement (April 2014) that a new arbitration centre – the Saudi Centre for Commercial Arbitration – will be established in Riyadh, possibly with branches outside of Saudi Arabia (including the UK). Full details are yet to be released, but the announcement demonstrates the commitment of the Saudi Government to nurturing arbitration as vital to continued foreign investment in KSA. The Centre will have its own set of local arbitration rules, tailored to the requirements of the 2012 Arbitration Law; this will greatly streamline the domestic arbitral process by avoiding the need to rely on international arbitration centres, and their respective rules. Moreover, parties still wishing to arbitrate disputes at centres outside KSA will have recourse to the 2013 Enforcement Law as a means of recovering sums awarded.

In conclusion

Although the enactment of the 2012 Law has provided an element of comfort to investors, and greater certainty of outcome should a dispute arise, there remains work to do. Two years on, the trend remains for arbitration concerning Saudi contracts to be seated in foreign centres and there are relatively few Saudi arbitrations: largely due to the inevitable lead time after parties began writing the 2012 Law into arbitration clauses.

Further measures are being put in place to improve the situation (as outlined above), after which KSA will be in a better position to establish a stronger track record of arbitration; giving foreign investors increased confidence that that the Kingdom is a good place to do business. In the meantime, parties should beware of the fault-lines in the existing legal framework.

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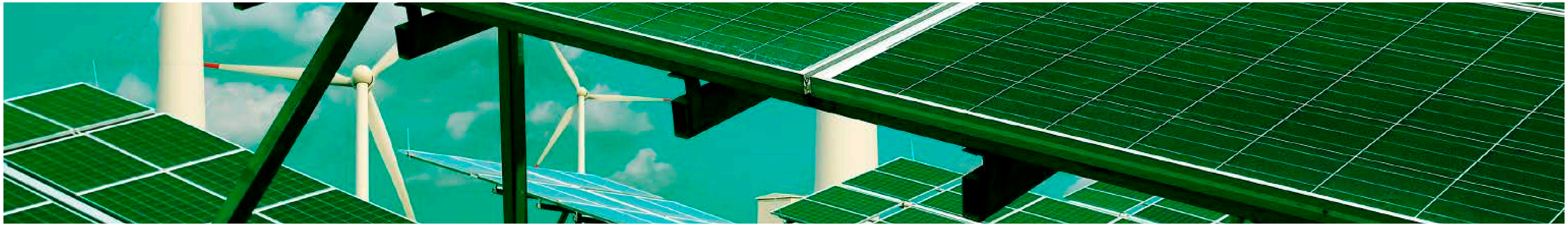
[2] Deloitte, GCC Powers of Construction 2012 – Construction sector overview



The challenge of energy infrastructure: energy security, decarbonisation and affordability

By Clare Hatcher

The UK energy system faces a number of challenges as existing infrastructure closes, domestic fossil fuel reserves decline, and the system increasingly requires adaptation in order to meet low carbon objectives. Changes are required to ensure that the UK has a secure energy supply in years to come and, already, the threat to supply security has been brought to the top of the agenda this year due to the political troubles in the Ukraine.

Background

The UK government has recognised that changes are critical to maintain security of supply and deliver the energy people need, where they need it. In its own words "*Large-scale investment is required in order to achieve security of supply as the UK makes the transition to a lower – carbon economy*".[3]

This is reflected in the fact that GBP 147 billion of the total GBP 375 billion required investment in the National Infrastructure Plan (NIP) is earmarked for electricity generation. In fact there is a view that this may not be enough. A joint report by the London School of Economics (LSE) and nPower suggests that the energy sector needs record levels of investment of up to GBP 330 billion by 2030 if security of supply is to be achieved while carbon emissions are reduced. This in turn would enable the UK to achieve the EU's long term 2030 emissions reduction target.

Where is the energy investment required?

HM Treasury's "National Infrastructure Plan: finance update March 2014" (Treasury Update) accepts that the historical model of large utilities financing electricity generation on balance sheet is unlikely to deliver the scale of investment required. This is particularly the case when the traditional utilities are seeking to reinforce their balance sheets through asset sales and cuts in capital expenditure[4]. As a result, the way forward must include project specific investment in the electricity sector with finance through separate vehicles where the return is directly related to the performance of specific electricity assets.

The Treasury Update gives a useful summary of where investment is required and the total value of projects (by technology type) which are in the pipeline for the period up to 2020 (excluding those in construction or already part of an active programme).

Nuclear

It is no surprise that a sizeable chunk of funds are required for Hinkley Point C, which is the first nuclear plant in the nuclear renewal programme regarded as essential to ensuring that the UK has a secure and low carbon electricity supply. In order to give investors the confidence to commit the billions necessary, the UK government has provided price certainty through contracts for difference for the power off-take at what is generally regarded as a very generous strike price. It also intends to provide support through the UK Guarantees Scheme.

Off-shore and on-shore wind

The off-shore wind sector potentially offers the largest investment opportunity pre-2020 with an estimated value of GBP 18.3 billion. On-shore wind, which is thought to have an existing established investment model using debt markets, is expected to generate projects with a value of up to GBP 10.4 billion. There is also help for developing offshore marine renewable energy (both tidal and wave) through demonstration projects such as the publicly owned Wave Hub in Cornwall.

Other renewables

While large scale renewable projects may provide suitable investment opportunities for project specific finance, small scale renewable projects (including solar, wind and anaerobic digestion), are generally considered too small individually to be suitable for a project finance solution unless bundled up into a portfolio sale. The government intends to continue the support for smaller scale projects through measures such as feed-in-tariffs.

However large scale renewables (including solar) which have historically been supported through the Renewables Obligation regime, will continue to receive support as part of the government's Electricity Market Regime (EMR) policy through 'contracts for difference'.

Biomass

There is a GBP 900 million potential opportunity for investment in biomass where the government has supported conversion of one engine at Drax, the UK's largest coal power station, to biomass by providing a GBP 75 million UK Guarantee.

Gas

One of the key issues facing the UK energy market is the extent to which gas-fired capacity will be developed and a "dash for gas" will slow down the need for structural changes which are required to reduce carbon emissions. Although the construction of combined cycle gas turbines (CCGT) could result in short term price gains by switching from coal to competitively priced gas (while initially achieving moderate reductions in greenhouse gas emissions), this delays the long term investment required in low carbon plant if required emissions reductions are to be achieved.

It is interesting in this context to see that the government regards investment in CCGT as part of the energy mix. The Department of Energy & Climate Change's (DECC) EMR policy is to create a capacity market with 15 year capacity agreements available which should provide sufficient certainty to unlock investment in new gas plant. The government's recognition of the continued importance of fossil fuels as an important source of the electricity generation mix is also implicit in the allocation of GBP 1 billion of public funding to help develop Carbon Capture and Storage through a commercialisation competition.

Will investment be made?

The reality is that the government's energy and climate change policy has three competing objectives: energy security; decarbonisation; and affordability. These are enshrined in the Energy Act 2013 (Energy Act) which contains the legal framework for the government's EMR policy for long term support for low carbon electricity generation.

The conflict is reflected in the factors the government must take into account under the Energy Act when setting its decarbonisation target range. While the impact of climate change is relevant it must also consider the need for economic growth and the cost to consumers. There is no easy way to reconcile the fact that it costs more at the moment to provide power from low carbon technology than from traditional fossil fuel sources. The Labour opposition has politicised energy prices making it difficult to retain the current green levies which add a substantial amount to the cost of household bills. However some sting has been taken out of this debate by Ofgem's referral of the energy market to the Competition Markets Authority (CMA) who are unlikely to report until after the next election.

Given that the CMA's main focus will be to assess whether the "big 6" suppliers should be broken up, there are significant concerns that this will put a halt to the investment needed in UK power generation.

Despite this, there are a number of hopeful signs that investment to create green growth has started. A recent EY Renewable Energy Country Attractiveness Index[5] indicates that the UK is now the fifth most attractive place in the world for renewables, the second for biomass and the first for off-shore wind. Further, according to Bloomberg, Britain saw record levels of investment in renewable energy in 2012 to 2013 which rose 59% to GBP 7.3 billion; placing the UK third in the world behind China and the US.

Finally, in late April, the DECC announced the first tranche of support under the new legislative framework for eight major new renewable projects ranging from off-shore wind to the conversion of a unit at Drax to biomass which will attract around GBP 12 billion in private investment. This will be followed by auctions for 'contracts for difference' to assist the low carbon transition. The UK is also now benefitting from some foreign direct investment in its renewable supply chain with ABP and Siemens making a GBP 310 million investment in Hull in two new factories to make turbine blades and assemble off-shore wind turbines.

The future of UK energy depends on continued investment. This in turn depends on ensuring the investment environment is favourable and one of the key conditions that must be satisfied to enable development is regulatory certainty. With more clarity emerging on the detail of EMR and the announcement of the first awards for support, there may now be a base on which investors can rely to unlock their funds.

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[3] HM Treasury and Infrastructure UK: National Infrastructure Plan: Finance Update, 19 March 2014
[4] Industry Outlook, EMEA Electric and Gas Utilities. Moody's Investors Service, 20 November 2013
[5] Ernst & Young: Renewable energy country attractiveness index, February 2014

Top tips

Drafting or reviewing the terms of a contract

Time invested at the outset of a project in thoroughly drafting or reviewing the terms of a contract and getting it right is time well spent. Adopting even simple measures will go a long way.

Do's

- ✓ Establish a standing *"check list"* against which to undertake a contract review, so as to ensure the capture of issues such as: consistent rights and obligations between Employer and Contractor in relation to payment, suspension, termination and other similar clauses
- ✓ Aim for consistency in defined terms and between the terms used in different documents forming the contract
- ✓ Ensure that the scope of work that is described by the contract and specification is clear, unambiguous and explained in simple, straightforward terms

Don'ts

- × Avoid commencing work pursuant to *"Letters of Intent"* or *"Letters of Award"* wherever possible – or at least understand their limitations as to scope and enforceability
- × Do not over engineer the contract. A contract that consists of a consolidated set of documents is more likely to be read and properly administered than one that consists of multiple lever arch files, containing layers of conditions, specifications, attachments and correspondence each amending the other

Collateral warranties and third party rights

The main provisions of a warranty should always include an obligation to adhere to the terms of the underlying contract. The warrantor must owe the beneficiary a duty of care in respect of its professional design obligations.

Other common warranty provisions include:

- **Copyright licence** – granted in relation to the design work
- **Prohibition on the specification or use of "deleterious materials"** – watch for confirmations about other parties' use of materials
- **PI insurance** – usually for 6 or 12 years after the end of the services or practical completion
- **Beneficiary's right to assign** – often limited to a specific number of assignments
- **Step in rights** – usually funder only, allowing it to effectively take the place of the employer under the underlying contract
- **No prejudicial amendments (third party rights only)** – check the underlying document does not permit amendments to it which affect the beneficiary's rights

Common limitation provisions:

- **No greater liability clause** – seeks to put the warranting party at no greater legal risk under the warranty than it would have under the underlying contract
- **Equivalent rights of defence** – allows a claim to be defended using defences which would have been available to the warrantor under the underlying contract
- **Financial cap** – a limitation of liability to the beneficiary in a fixed amount
- **Net contribution clause** – limits the warrantor's liability to a fair and reasonable proportion where it may otherwise be held liable for the full amount of the loss in the first instance
- **Repair, renewal or reinstatement costs** – exclusion of all losses, other than the reasonable costs of repairing the building itself

Stop press:

New heads of construction for Australia and South East Asia practices

Clyde & Co is pleased to announce that senior construction partner, **David McElveney**, is to head the firm's fast-growing construction practice in Australia, having spent the last six years leading the projects and construction practice in Abu Dhabi. David will be maintaining a regional practice out of Clyde & Co's Sydney and Abu Dhabi offices.

The firm's Asia Pacific offering has also been boosted with the addition of Singapore based construction specialist, **Eugene Tan**, who leads the firm's South East Asia construction practice.

Clyde & Co opens new office in Southern California

We are pleased to announce that we are expanding our West Coast offering with a new office in Orange County, concentrating on the marine and energy markets.

Paris partner hires expands African projects capability

Clyde & Co has expanded its offering in the key industry sectors of infrastructure, energy and telecoms with the hire of two partners in Paris, **Carole Arribes** and **Eric Diamantis**. These new additions will enhance the firm's French commercial practice and cross-border capability, and the global projects & construction group in particular.

Clyde & Co to launch in South Africa

We are delighted to announce that we will shortly be opening offices in Johannesburg and Cape Town, which will initially cover dispute resolution and all classes of insurance business.

Guide to contracting in global markets

Covering 22 countries and regions in which we routinely act, our 'Guide to contracting in global markets' provides contractors around the world with a high level review of some of the key legal requirements and implications of operating in developed and emerging markets.

Click here to request your copy.

Exploring global infrastructure market opportunities event and summer drinks reception

Our global projects & construction group will be hosting a 'Dragons' Den' style event on Wednesday 9 July at our offices in London. Partners from Australia, South East Asia, Africa and the Middle East will be pitching to a distinguished panel of 'Dragons' to persuade them to invest in a particular infrastructure project in their region.

This will be followed by the group's annual summer drinks reception. **Click here** for further details.

UK Infrastructure in 2014 briefing

Find out about the future of investment driving projects and progress under the National Infrastructure Plan.

Click here to request your copy.

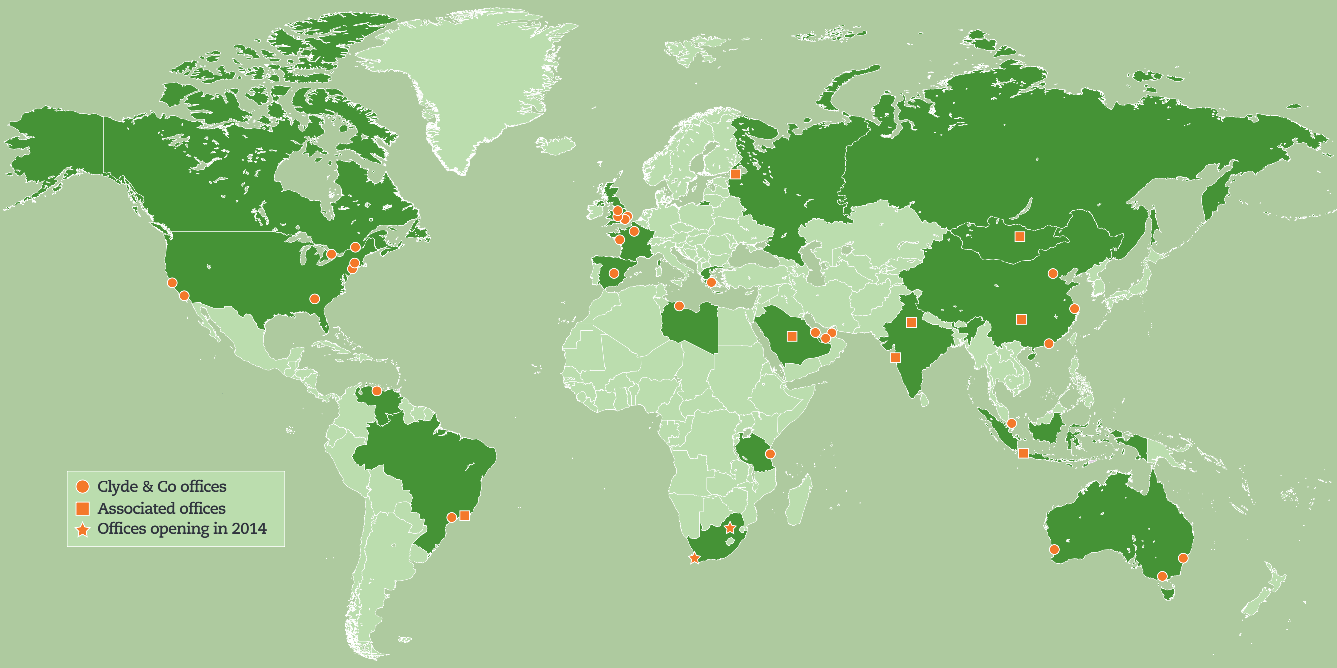
Clyde & Co advises Guinean government on USD 20 billion landmark Simandou South iron ore project

Clyde & Co has advised the Guinean government on the Simandou South iron ore mining project Investment Framework which was signed with Rio Tinto, Chinalco and The International Finance Corporation, a member of the World Bank, in Conakry, the Guinean capital, on 26 May 2014. The next step is the finalisation of the Bankable Feasibility Study in early 2015.

A number of specialist partners have worked on the corporate, rail and port infrastructure aspects of the project and the team includes lawyers from the firm's UK, Paris and Middle Eastern offices.

Due to start commercial production by 2018, it will be the largest integrated iron ore mine and infrastructure project in Africa, with the potential to transform the development of Guinea's economy and transport infrastructure.

Our offices



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Further advice should be taken before relying on the contents of this Newsletter.