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**Construction Contractors Association of Western Australia Inc**

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This Position Paper provides a summary of the CCAWA's Member endorsed approach proposed for the nominated Topic and is intended to be used as a guideline for all CCAWA member interactions, communications and other activities related to the nominated Topic.

**Topic:** Latent Conditions and Other Unknown Risks

**Context**

This Position Paper relates to all changes in contract scope that cannot be foreseen or quantified at time of tender (including latent conditions and other risks).

**Objectives**

Managing 'risk' is a significant part of project planning and execution. Many risks can affect the cost and time of project delivery. At the time of tender, some of these are known, some are known unknowns, some are unquantifiable and there are unknown unknowns.

At both the time of tender and during execution, the management of risk has to be equitable. Passing a risk that could generate a cost and / or delay that can neither be reasonably foreseen nor quantified should be avoided.

**Current Approach**

Many factors can affect the cost, time and quality of the outcome of a scope of work. These are generally referred to as 'risk' and can include:

- Factors controlled by the contractor (eg. productivity)
- Factors controlled by the client (eg. approvals and access to the site)
- Factors that are controlled by neither (eg. weather), and / or
- Factors that are unquantifiable (eg. subsurface conditions).

Whilst the management of risk should fall to the party that is best placed to manage that particular risk, the cost and time of mitigating and managing risk are generally placed with the contractor, and often with little or no entitlement to the time or costs associated. This effectively asks the contractor to 'gamble' on an outcome. This approach is unsustainable for the Industry.

**Key Issues and Factors**

Risk transfer without compensation to the contractor has become more and more prevalent and any typical tender process creates competitive tension that encourages contractors to take on unquantifiable risk or face the prospect of losing.

In order to combat this tension, Australian Standard Contracts were developed to be fair and reasonable to both parties. Over time however and unfortunately as can be found in case law, AS2124 (1992) included a particular a drafting error that tended to favour inexperienced contractors because it included a 'subjective test' of what a contractor should know at the time of tender. As a response, some clients amended the clause significantly. As a result Standards Australia drafted AS4000 (1997) to provide for an objective test. Recent case law has shown that neither clause is perfect (See Appendix 1).

Importantly, the latent conditions clause (amongst others) is intended to deal with unexpected and unquantifiable conditions. However it is still being amended significantly to place unquantifiable risk with the contractor.

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Although clients may be tempted to try to transfer as much risk as possible to the contractor, this will often be a false economy as contractors will often make allowances for that risk in their pricing, which could result in the principal paying a premium for risks that never eventuate. Alternately, this approach can lead to Contractors signing up to unprofitable contracts that drain resources and invariably cause delays to Clients and their projects.

This shows the importance of having a transparent 'meeting of the minds' in managing and compensating for unforeseen or unquantifiable events.

#### CCAWA Proposed Approach

We are advocating for an approach that recognises fixed prices require fixed scopes and that 'acting in good faith' as is required under AS4000 requires that unquantifiable scope cannot by definition be included in a fixed price contract.

This new paradigm must include a simple test – are the commercial interests of the parties aligned?

The CCA is not advocating all care no responsibility for the contractor and encourages the use of latent conditions provisions similar to those in AS4000 or other well documented standard form contracts.

Risk workshops at the time of tender should involve discussion on how risk is going to be managed, who is best placed to manage it and how it will be priced and scheduled in the event that it occurs.

Scope changes due to unforeseen events should be managed in alignment with the commercial interests of the parties.

#### Outcomes

Where the parties cannot foresee a project risk or are unable to quantify that risk then the resolution must be both transparent and reasonable. A starting point is the adoption of a standard latent conditions clause like AS4000.

### Appendix 1 - Latent Conditions clauses

Clause 12 of **AS2124-1992**:

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Clause 25 of **AS4000-1997** provides:

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