EIC SPRING GENERAL ASSEMBLY

How contracting models are responding to global trends in the construction sector

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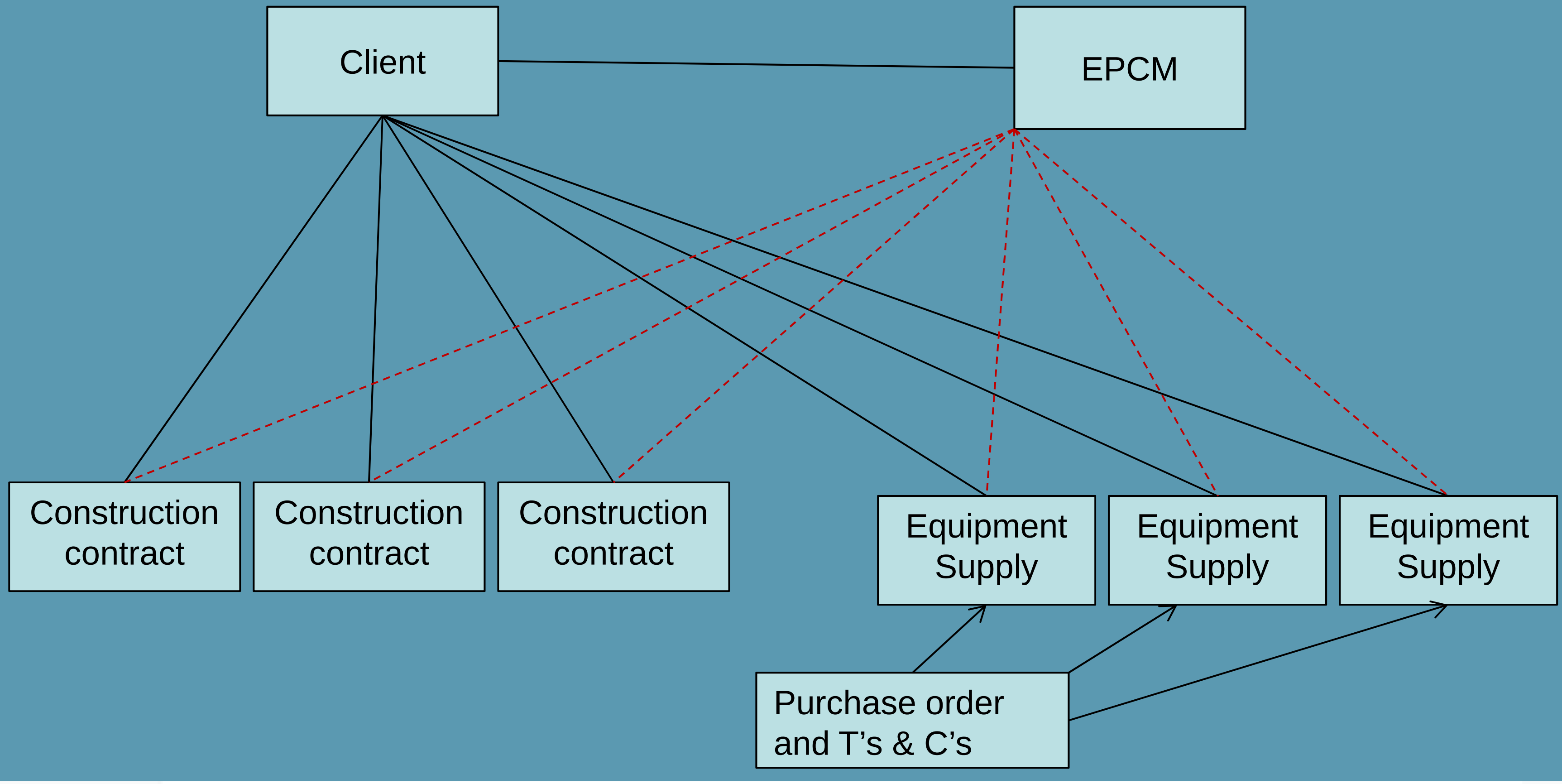
Trend: Bigger and more complicated projects

Effects:

- PQQ Requirements increasing/projects becoming multi-faceted leading to:
  - more joint venture arrangements/consortia or mergers – implications for contracts
  - longer tender periods – risk of abortive costs and protection of know-how
  - staged projects – e.g. development of design to FEED then fixing of price/design and build/EPC turnkey (with option for employer to abort)
  - multiple (and multi-disciplinary) packages – interfaces, different skill sets, more “EPCM” arrangements or “mixed EPC models”

Mixed Contracting Models

Traditional "EPCM" model



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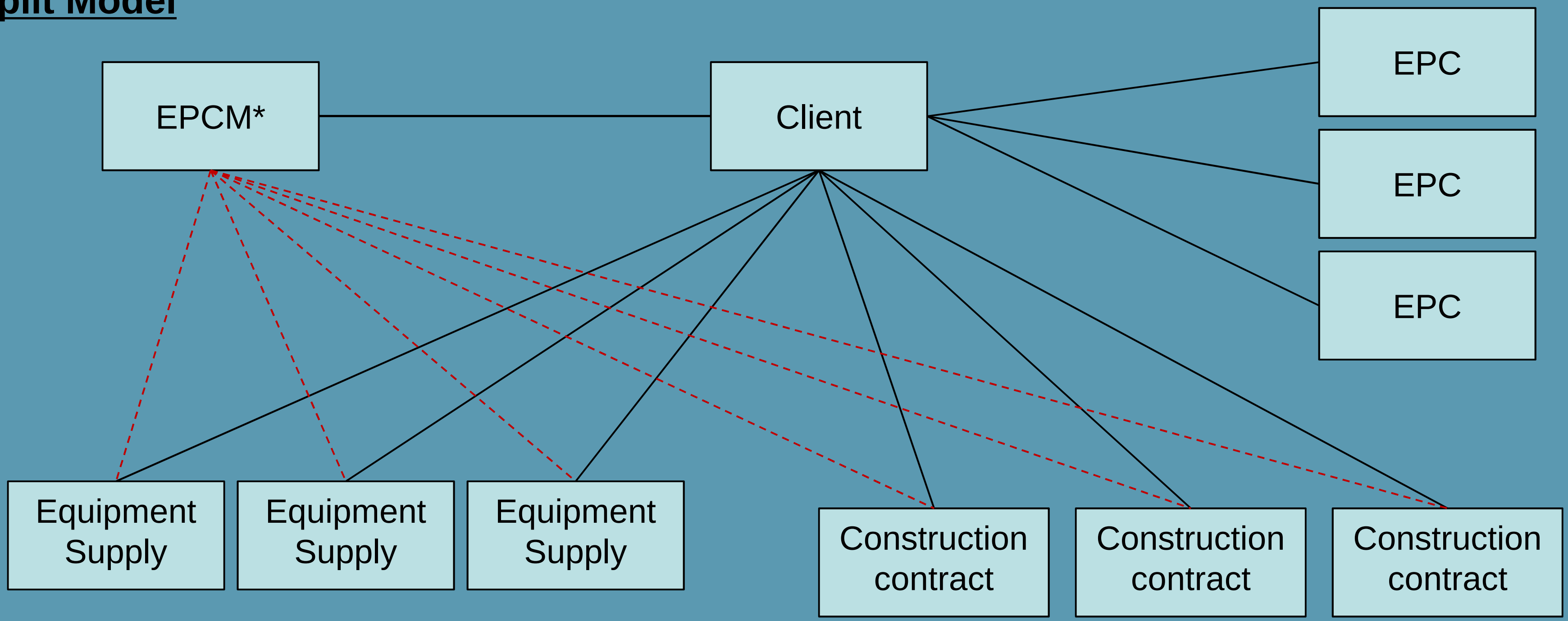
Mixed Contracting Models

Split Model



* “E” & “P” can be split from CM with CM undertaken by Client in house or by another consultant (for cost savings)

Trend: Bigger and more complicated projects (cont.)

- Longer construction periods (insurance and other implications including maintenance of performance security)
- Longer defects liability periods mixed with optimisation/maintenance obligations – on the positive side more O&M opportunities?
- Cost drivers resulting in:
  - Greater use of incentivisation models – what next – alliancing?
  - PPP's "to be or not to be"? (Public sector struggling with budgets to plug infrastructure gap)
- Continuing role of standard forms but will they meet the challenges?
  - Deviate from domination by one standard form (e.g. FIDIC). Potential rivals: NEC, Australian models (especially re: alliancing) <u>or</u> more bespoke solutions?

Trend: More demands on the sector

Effects:

- Increasing awareness of payment/performance security and cash flow:
  - Evidence of employer's financial arrangements (e.g. FIDIC)
  - Letter of credit
  - Neutral to positive cash flow; increasing use of payment milestones
  - Robust termination provisions
- Security of performance security:
  - Subcontractor Collateral Warranties, Performance Bond and Parent Company Guarantee now standard
  - On international scene – On Demand bond typical

Trend: More demands on the sector (cont.)

- Political security:
  - Termination regime (robust termination rights and compensation)
  - Change of law provisions
  - Increase in Investment Treaty awareness (positive)
- Security of supply chain – preferred suppliers, responsibility for delay/default, defects liability

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More demands on the sector (cont.)

- Social licence provisions – e.g. welfare, sustainable development, human rights
- Bribery and corruption – international obligations
- Global impact of international events – increasing focus on force majeure clauses (e.g. swine flu, Ebola)
- Greater focus on dispute avoidance/resolution and “collaboration” (positive)

Trend: Bring your own finance

Effects:

- Different models, e.g.:
  - Equity investment
  - Delayed cash flow/loan facility
  - Alliancing – sharing risk (but also the upside)
  - Staged projects – with some of initial design development being taken on risk
  - PPP's

Conclusions

- A mixed bag: positive and negative
- More innovation – with this comes opportunities and an ability to develop a USP and beat the market
- Revisiting of corporate "bottom lines" but flexibility will set you apart from competitors

"It is not the strongest or the most intelligent who will survive but those who can best manage change"

Charles Darwin

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