

## GLOBAL CONSTRUCTION

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## LNG CONSTRUCTION BLOWOUTS TURNS TO BONANZA FOR DISPUTE LAWYERS

Australia's liquefied natural gas sector is set to be swamped by a multibillion dollar wave of disputes between producers and contractors over liability for cost blowouts and delays, as the slump in resources investment and commodity prices sharpens appetites to claw back funds.

Chevron's over budget \$US54 billion (\$AUD71.8 billion) Gorgon LNG venture, Santos' \$US18.5 billion (\$AUD26.3 billion) GLNG project and Inpex Corporation's \$US34 billion (\$AUD48.4 billion) Ichthys project in Darwin are among those understood to be the subject of arguments over responsibility for contract variations that have had an impact on the entire supply chain.

"The numbers are mind blowing," KordaMentha forensic expert Owain Stone said.

The gas companies leading the projects declined to comment. But Kevin Berg, general manager at Gladstone for Bechtel, the U.S. contractor building all three of the Queensland LNG plants as well as Chevron's Wheatstone project in Western Australia, played down the claims.

What makes the LNG sector unique is the sheer magnitude of the sums involved. Seven giant LNG projects, costing about \$AUD193 billion (\$US292.9 billion), are due to reach completion in the next two years, a [Australian] Department of Industry and Science snapshot of major resources and energy projects shows.

Law and accounting firms look to be the big winners of wrangles between producers, contractors and subcontractors over liability for changes to work orders that have in some cases pushed projects billions of dollars over budget.

One legal source pointed to three claims each involving more than \$AUD1 billion (\$US1.5 billion) and others that involve several hundreds of millions of dollars.

"This will create a bed load of work for those with the right expertise that will last several years," one legal source said.

Big law firms Corrs Chambers Westgarth and Norton Rose Fulbright have been gearing up for the past two years in anticipation of large complex disputes arising in LNG.

Corrs has hired two top shelf infrastructure litigation partners, Andrew Stephenson and Michael Earwaker and EY has raided rival Deloitte for one of its best brains in this field, Campbell Jackson.

Norton's legal eagles – led by construction lawyer Matthew Croagh – have been embedded with clients' project teams on LNG projects in Queensland, helping them "control costs".

"This work has been substantial for us," Mr. Croagh said.

Ron Finlay, a former managing partner of Corrs Chambers Westgarth and chief executive of Finlay Consulting, said oil and gas compared unfavourably with transport projects, where dispute resolution boards were now typical.

"Oil and gas has gone backwards, back to the bad old arbitration and litigation days," said Mr. Finlay, who is also the secretary of the Australasian division of the Dispute Resolution Board Foundation.

"A lot of those projects are under the control of very large U.S. EPC [engineering, procurement and construction] contractors. They like to have total control of the project and don't like other people telling them how to do their business; it's very much a client control process."

The oil price slump, which has dragged down LNG prices, has made project proponents keener to escalate claims into disputes, as has the increased depth in the construction market in recent years because they are less worried about creating bad blood with a particular contractor, one lawyer said.

"Boards are becoming more willing to take the gloves off where they feel they have been wronged by a contractor," he said.

Matt Fehon, a partner in McGrathNicol, which specialises in forensic accounting, said project principals and contractors were looking first to contain costs and then at how to recover them if there had been any non-compliance, scope creep or simply overcharging.

"That has led to a large number of matters that have been either litigated or arbitrated in the arbitration courts," Mr. Fehon said.

It is believed some construction firms have forensic accountants working on a success fee basis, using sophisticated data analytics to trawl contracts looking for inappropriately allocated costs.

The issue comes amid heightened concerns over construction costs in Australia, where vast investment is required for infrastructure projects and which overseas executives single out as already the most expensive country in the world for building.

The stretched construction market during the resources boom contributed to the problems, when producers were fiercely competing to get the "A" construction team but sometimes were lucky to get the "B" or "C" team, lawyers said.

"It was aggressive contracting in the boom times, then a focus on trying to deliver projects and get the thing done, average contract management, and then a scenario at the back end where there were overruns and contractors trying to get even more out of it because their workflow going forward was looking worse and worse," said one lawyer who is working on three separate disputes.

A dispute emerging between two parties typically triggers claims further up and down the chain as all parties seek to claw back money, with potentially scores of subcontractors involved on a project such as Gorgon, or Gina Rinehart's Roy Hill iron ore venture in Western Australia. Cases can last years as parties respond with exorbitant counterclaims, requiring a lengthy process to reach a settlement and creating a wealth of work for law and accounting firms.

This is driving a "land grab" to secure the best lawyers, barristers, arbiter panels, as well as seasoned forensic accountants with experience in the witness box.

Several high-profile disputes have already hit the headlines, particularly at the ultra-complex Gorgon project. A dispute between South Africa's Murray & Roberts and dredging company Boskalis over construction of a materials offloading wharf at Gorgon was settled in mid-2014 for an undisclosed sum. AJ Lucas also suffered losses on a contract for Gorgon, while Marine & Civil fell into administration after losses on project works on Barrow Island.

The management of CIMIC, formerly Leighton Holdings, has declined to specify the size of claims it is negotiating but legal filings from former employees reveal that management has been pursuing \$AUS1.46 billion (\$US1 billion) of claims from Chevron for work on a jetty for Gorgon.

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CIMIC and Chevron have been negotiating claims for years, with the U.S. energy major rejecting most of the claims on alleged cost blowouts, according to former employees.

Earlier this year, UGL and its American partner CH2M Hill each set aside \$US175 million (\$AUD178 million) for provisional write downs on a \$AUD550 million (\$US386.1 million) power plant built at the Ichthys site in Darwin. Project proponent Inpex is understood to be defending claims that the geotechnical data it supplied was inadequate.

Monadelphous is pursuing more than \$AUD200 million in claims to recover costs associated with “changes in scope and nature of the works” for a jetty, ship berth and ship loader it built for Wiggins Island Coal Export Terminal together with Malaysia’s Muhibbah Construction.

Pressure on contract delivery teams to meet aggressive timetables agreed by their bid teams have contributed to the problems.

“Time equals people and resources and machinery, and there’s a cost to that every day that ticks by,” Mr. Fehon said.

“In the case of a number of projects that could be marine vessels that run into the tens of millions for each month or period you have them on hire.”

A substantial portion of LNG related disputes that reach formal arbitration will be dealt with in the Singapore International Arbitration Centre, which is chaired by an Australian, Michael Pryles. Domestic law firms are frantically trying to capture construction and engineering litigation work before it goes overseas.

Mr. Finlay said transport projects had “seen the light” in their use of dispute resolution boards, which have become usual on government road and rail projects in Queensland and New South Wales.

Lindsay LeCompte, executive director of the Australian Constructors Association, said dispute resolution boards came at a cost because the parties had to pay for the experts.

“But at the end of the day, it’s not a cost that’s significant,” he said, adding that spending a few hundred thousand dollars on experts to prevent a \$1 billion contract blowing out 5 or 10 per cent above budget was worthwhile.

## ABOUT THE AUTHORS

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