



Key project and
procurement concepts

01 A strategic approach to construction contract preparation

Investing in Energy Transition Projects
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The nature of construction contracts

Purpose

The purpose of this paper is to explain the characteristics of construction contracts that are essential to understanding how and why they should be drafted by reference to the guidelines contained in other papers in this series.

Why are construction contracts different?

Construction contracts have a number of unique characteristics that bear on their drafting, interpretation and use.

Those characteristics include the following:

- **Long term:** Construction contracts are not instantaneous transactions. They deal with relationships that last for years, from the conception of a project through to its operation and maintenance.
- **Dynamic:** Construction contracts deal with dynamic events and ever changing circumstances. They must be prepared so as to assist the parties through those conditions and govern, with certainty, a range of events that are foreseeable and some which are not.
- **Numerous stakeholders:** The construction process involves many stakeholders: clients, contractors, subcontractors, suppliers, governments, financiers, offtakers and purchasers and community groups.
- **Value:** Projects range from tens of thousands of dollars to billions of dollars and are often of great social and economic importance.
- **Complexity and uncertainty:** Projects are complex. They involve many people, numerous disciplines and complex technologies. They are also uncertain. Often, the contract sum and Programme can be based on a wide range of assumptions and guesses. The construction contract must deal with the consequences of those assumptions being incorrect.
- **International:** Contractors and suppliers are often international and are influenced by the practices of their home countries.
- **Disputes:** When these issues are combined, disputes are understandably frequent in construction contracts.
- **People:** Most importantly, construction contracts must regulate complex interactions over a prolonged period by people. That's the tricky bit.

What must construction contracts do?

All construction contracts must deal with the issues set out above and other complex factors in a manner that is legally certain, able to be used effectively by the parties and is commercially sustainable.

The contracts will establish a set of rules that can be used by the parties to manage their relationship as the project unfolds and that guides them when disagreements arise.

In doing so, construction contracts will regulate matters such as:

- the scope of works and services to be carried out and their variation
- the purposes that must be fulfilled
- time and its extension
- payment and financial adjustment
- unforeseen intervening events
- compliance with laws
- the consequence of breach
- the management of disagreements.

All of these complicated matters must be taken into account by the parties when approaching their relationship.



Strategic contracting on an end to end basis

Purpose

The construction process is complex and lengthy. Construction contracts are entered into as a means of assisting the parties to achieve the goals they have when embarking on a project. The preparation of construction contracts and the organisation of the project must be based on a strategic analysis of the requirements for project success and the challenges that might be encountered.

What is project success?

Project success can be defined as the delivery of the project in circumstances where:

- the projections as to the time and cost of project delivery that are the basis of the investment decision have been achieved
- quality and reliability are to specification
- social, safety and environmental standards have been met
- there are no material unresolved claims that require dispute resolution.

In a positive sense, the contracting strategy should have a material effect on the achievement of those outcomes.

In a negative sense, the contracting strategy should not be an impediment to them.

If the elements of project success are not all met, the project might not be a complete failure, but it will have resulted in waste because the investment of time, money and effort has not resulted in the required positive outcomes to the fullest possible extent.

Sources of project failure

Projects can fail for many reasons. However, experience indicates that a combination of the following factors are usually material contributors:

- inadequate scope definition
- unrealistic Principal expectations
- failure to identify and develop strategies for key project risks
- changes in personnel
- poor communication
- lack of problem solving skills and processes
- absence of predictive planning tools
- poor contractor or consultant selection.



Methodology

Taking into account the requirements for project success and the sources of project failure, the following template can be used as a tool in developing an effective project delivery strategy.

Planning phase	Contracting phase	Delivery phase	Resolution phase
<p>Commercial and other project goals</p> <p>Have the commercial and other project goals and their priority been clearly explained?</p>	<p>Tender strategy</p> <p>Have there been pre-tender market soundings?</p> <p>Is pre-qualification appropriate?</p> <p>What is the critical information required in order to make an informed choice?</p> <p>What is the best approach to maintain competitive tension?</p> <p>Have clear offers been obtained?</p> <p>To what extent is pushback on contractual terms critical?</p> <p>Have any contractual terms attracted premiums in relation to risks that could be better managed by amended terms?</p> <p>What is the level of confidence in the contractor's ability to perform in accordance with the contract?</p>	<p>Processes</p> <p>Are the processes in the contract feasible and useful?</p> <p>Have effective processes been established in relation to:</p> <ul style="list-style-type: none"> • time • cost • variations • defects • completion • claims? <p>Governance</p> <p>Does the contract provide for effective project governance, including between contracts (where there are interfaces) and at a strategic level?</p> <p>Information</p> <p>Does the contract provide for the provision of all information required to monitor performance and other factors relevant to project delivery?</p> <p>Personnel</p> <p>Are all personnel performing in a competent and constructive manner?</p> <p>What can be done where that is not the case?</p>	<p>Strategic issues</p> <p>What is the capacity of the Principal to participate in a significant dispute?</p> <p>What would be the effect of a significant dispute on the project?</p> <p>What are the most likely sources of dispute, particularly in relation to:</p> <ul style="list-style-type: none"> • the Programme • technology • cost • interface • variations • defects • under-performance? <p>Does the Principal have adequate self help remedies, such as security and set off in the event of a dispute, especially taking into account SOPA?</p> <p>Processes</p> <p>Are the dispute resolution processes suitable for the different types of disputes that might be encountered?</p> <p>Do the claims and dispute resolution processes encourage the exploration and resolution of the issues or do they shunt the parties into proceedings?</p>

Methodology

Taking into account the requirements for project success and the sources of project failure, the following template can be used as a tool in developing an effective project delivery strategy.



Planning phase	Contracting phase	Delivery phase	Resolution phase
<p>Performance and other technical requirements</p> <p>What project technical outcomes must be achieved in order to achieve the project goals?</p> <p>Are they realistic or stretch targets?</p> <p>Is new technology involved?</p> <p>To what extent have the engineering specifications required to achieve the technical outcomes been finalised?</p> <p>What is the extent of scope uncertainty?</p> <p>What is the pathway to scope certainty?</p>	<p>Contracting strategy</p> <p>Do the contracts manifest the requirements for project success in a reasonable, feasible manner?</p> <p>If the scope is not certain, does the contract recognise the pathway to scope certainty?</p> <p>If not, how and by when will the scope be made certain?</p> <p>Is any residual scope to be performed by the Principal clear and able to be satisfied by the Principal by the required times?</p> <p>Have the consultancy agreements been prepared on the basis that they are to be novated?</p> <p>Are the scopes and terms of the consultancy agreements suitable for novation?</p> <p>Do the contracts deal with the requirements of financiers and other stakeholders?</p>		



Methodology

Taking into account the requirements for project success and the sources of project failure, the following template can be used as a tool in developing an effective project delivery strategy.



Planning phase	Contracting phase	Delivery phase	Resolution phase
<p>Budget constraints</p> <p>Is the project budget known and what are its tolerances?</p> <p>Is it realistic?</p> <p>If not, where is it vulnerable?</p>	<p>Risks and responsibilities</p> <p>Is the risk allocation clear and sustainable?</p> <p>If neither party can control the risk but it is allocated to one party, how is that risk to be managed?</p> <p>Where risks are to be shared, are the price and time mechanisms adequate?</p> <p>Do the contracts and the associated specifications set out all of the responsibilities required for project delivery?</p>		
<p>Programme constraints</p> <p>Are the overall Programme requirements known?</p> <p>Are they realistic?</p> <p>If not, where is it vulnerable?</p>	<p>Interfaces</p> <p>Does the project entail inter-contract interfaces?</p> <p>If so, how are those interfaces managed?</p> <p>Is the risk allocation in relation to them feasible?</p>		
<p>Resources</p> <p>What resources will be required?</p> <p>To what extent can they be provided by the Principal?</p> <p>Are the other resources available?</p>			



Methodology

Taking into account the requirements for project success and the sources of project failure, the following template can be used as a tool in developing an effective project delivery strategy.



Planning phase	Contracting phase	Delivery phase	Resolution phase
<p>Known risks</p> <p>What are the key known project risks?</p> <p>Have any risk mitigation strategies been developed?</p> <p>Are lessons learned from comparable projects available?</p>			
<p>Potential for unknown risks</p> <p>Is the project such that there is an unusual susceptibility to unknown risks, such as ground conditions, technology failures or political interference?</p>			
<p>Financier requirements</p> <p>Have financier requirements been taken into account?</p>			
<p>Other stakeholder requirements</p> <p>Who are the other key stakeholders, such as governments and community group and have their interests been taken into account?</p>			



How to contact us



If you have any questions about this paper, please contact the editor, Damian McNair, Partner, Energy Transition.

PwC Australia has a dedicated Energy Transition business, consisting of a hub of 132 multidisciplinary and highly-skilled experts helping to facilitate Australia's successful transition to a decarbonised economy by 2050. We are helping accelerate our clients through the energy transition and their related ESG priorities as Australia moves to a net zero economy.

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