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Project Alliances

*Graham Thomson**

SUMMARY

Project alliancing is a new and novel strategy for delivering major projects. Of all the new approaches to the delivery of construction projects, project alliancing is the most innovative and it challenges many attitudes and practices which have long been entrenched in the industry. Project alliancing was first adopted in offshore oil and gas projects in the North Sea and has now extended into the mining and onshore resources industries. To date, three major projects in Australia have adopted the project alliancing strategy; namely, WMC Petroleum's East Spar Project, Ampolex's Wandoo Project and BHP Direct Reduced Iron's Port Hedland Project.

This paper deals briefly with the traditional approaches of delivering a construction project and the emergence of new approaches, but focuses primarily upon project alliancing. It covers:

(a) the history of project alliancing;
(b) the principles of project alliancing;
(c) the contractual structures of project alliances;
(d) the commercial drivers;
(e) sub-alliancing/sub-contracts; and
(f) the role of lawyers and facilitators in project alliances.

The paper notes that, to date, alliancing has been adopted primarily on large-scale projects and with "blue-chip" companies as the alliance participants. These companies have all had many years of experience with various forms of contracting strategies and have decided that for certain major projects alliancing is the appropriate contracting strategy. The paper concludes that while project alliancing is not a panacea, it is certainly making its mark in major project work, and continued good results from alliancing will ensure its future as a desirable delivery strategy for major projects.

INTRODUCTION

This paper focuses on project alliancing, which is a new and novel strategy for delivering major projects.

Project alliancing was adopted, first, in offshore oil and gas projects in the North Sea, and has now extended into the mining and onshore resources industries. To date, three major projects in Australia have adopted

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the project alliancing strategy; namely WMC Petroleum's East Spar Project, Ampolex's Wandoo Project and BHP Direct Reduced Iron's Port Hedland Project.

This paper deals briefly with the traditional approaches of delivering a construction project, and the emergence of new approaches, but focuses primarily upon project alliancing.

First, however, some definition of terminology is essential, as the words "alliancing", "partnering" and so on mean vastly different things to different people.

"Partnering": This term is confined to the concept of a "handshake" arrangement running in parallel with a fairly traditional contract, a concept spearheaded in the construction industry by Charles Cowan of the Associated General Contractors of America (and formerly of the United States Corps of Engineers) and fairly widely used in Australia.

"Strategic partnering/strategic alliancing": While strategic partnering/alliancing are "loosely defined concept[s] that can be used to cover a wide range of diverse commercial arrangements between two or more organisations",[1] the NEDC report *Partnering, Contracting without Conflict*[2] defined strategic alliancing/partnering as:

> "a contractual arrangement between a client and his chosen contractor which is either open-ended or has a term of a given number of years rather than the duration of a specific project. During the life of the arrangement, the contractor may be responsible for a number of projects, large or small and continuing maintenance work or shutdowns. The arrangement has either formal or informal mechanisms to promote co-operation between the parties."

While the core characteristic of strategic partnerships/alliances appears to be "trust and teamwork",[3] the key elements of a strategic partnership/alliance have been stated as:

(a) two or more firms uniting to pursue a set of agreed goals, but remaining independent subsequent to alliance formation;
(b) those firms sharing the benefits of the alliance/partnership and controlling the performance of assigned tasks; and
(c) those firms contributing *on a continuing basis* in one or more key strategic areas.[4]

"Project alliancing": The bringing together of an integrated team comprised of the "best people for the job", drawn from the organisation of each of the alliance participants for the purpose of delivering a particular project is what is meant in this paper by "project alliancing".

As the name implies, the distinguishing feature of a project alliance is that it is project specific. As this paper is focused on project alliancing, it is generally simply referred to as "alliancing".

[1] Singleton, "Partnering for the Public Sector: Guest Editor's Introduction" [1994] 53 AJPA 1.
[2] (June 1991).
[3] Singleton, op cit n 1.
[4] Yoshino and Srinivasa Rangan.

THE TRADITIONAL APPROACH

The traditional contract model is as per Figure 1.

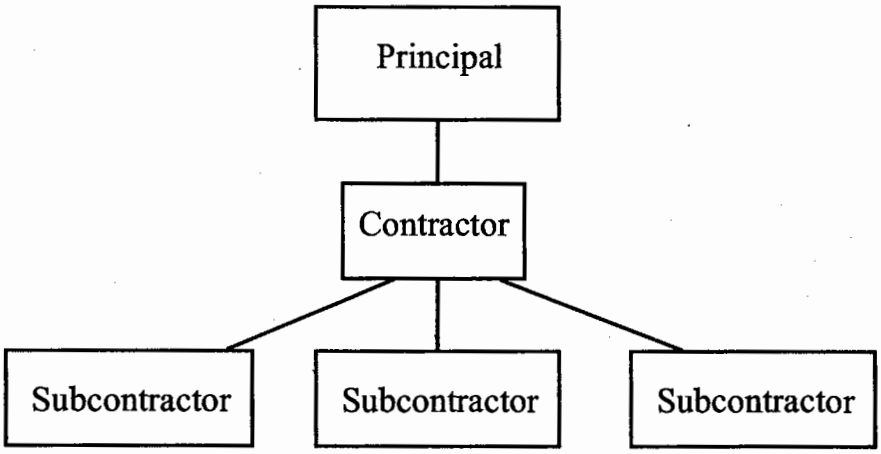

Figure 1: Traditional contract model

Some of the advantages and disadvantages of traditional contracting (from the principal's point of view) are as follows:

Advantages	Disadvantages
• Fixed lump sum	• Adversarial relationship
• Clear risk allocation	• "Claimsmanship" (ie, low tender price but large claims during contract period)
• Staff familiarity with contracts	• Lack of trust
• "Draconian" clauses	• "Draconian" clauses
• Competitive tenders deliver lowest price	• Lack of open and honest communication

While there are certainly no hard and fast rules as to the best contracting strategy to adopt, a number of major companies have decided that, for particular important projects, the disadvantages of the traditional contracting model outweigh the advantages. For example:

BP Exploration Europe (BP) – Hyde and Andrews Projects

According to Bob Scott,[5] the traditional form of contracting had led to developing relationships with BP's contractors which exhibited the following features:

(a) short-term and essentially adversarial in nature;
(b) unaligned objectives;

[5] Scott, *Partnering and Alliance Contracts: A Company Viewpoint* (April 1994).

(c) accountabilities not clearly defined;
(d) risks placed on those unable to influence or manage them; and
(e) skills not recognised and/or inefficiently used.

All of these were perceived by BP to characterise a "master/servant" relationship and to be major contributors to inefficiencies. It was clear to BP that "whilst there was no single panacea for the industry's ills, changes in behaviour and relationships by and between all parties would be critical to future success".[6]

Ampolex-Wandoo Project

David Minns[7] notes that Ampolex's decision to alliance arose from concerns that a traditional contracting strategy would not deliver a satisfactory result, due inter alia to:

1. organisational issues: Ampolex had a philosophy of maintaining a flat company structure and keeping staff numbers as low as possible.
2. cost control: Ampolex was keen to avoid costs arising from duplication of activities and felt, on a more general level, that traditional contracting did not encourage contractors to use their expertise to reduce costs.
3. undue exposure: Ampolex owned 100 per cent of WA-202-P and felt that good risk management demanded that this exposure be reduced.
4. confrontational relationship: It was believed that the client/contractor relationship would not achieve outstanding results. A disproportionate amount of energy would be expended arguing over claims rather than managing the project. In fact, a major construction project was starting to be seen as a prelude to a protracted piece of litigation.

WMC: East Spar Project

Peter Campbell[8] observed that in WMC's view, the traditional contracting model was ill-suited to WMC's need to optimise the development concept without delaying the project. On that project, while a base case development plan (sub-sea wells with a tripod gathering platform) was approved, alternative, less proven concepts, including an all-sub-sea scheme, required a longer period to prove-up technically and evaluate economically. WMC required the flexibility to vary the development concept while maintaining schedule and cost.

BHP Direct Reduced Iron: Port Hedland Project

BHP let its initial construction contracts on a traditional basis, but decided that the disadvantages of the traditional contracting strategy were such as to give rise to serious concern as to its ability to complete construction on time and within budget.

[6] Ibid, p 3.
[7] Campbell and Minns, "Alliancing — The East Spar and Wandoo Projects" (1996) 15 (4) AMPLA Bull 202.
[8] Ibid.

McDermott Engineering (Europe)

While noting that it is a question of "horses for courses", Peter Wilson[9] has observed that the traditional contracting model is not well suited for projects which are inherently fast tracked and very focused and which may need to be arranged at short notice, outside the normal process of competitive bidding.

CRINE Report[10]

The CRINE Report on the oil and gas industry attacked a number of aspects of the traditional contracting model and recommended the simplification and clarification of contract language, the elimination of adversarial clauses, encouragement for risk/reward relationships and the curtailment of liquidated damages. The report notes that "manning and mistrust is one of the largest and most futile cost drivers of all".

NEW APPROACHES

As Scott has noted, on North Sea development projects virtually every conceivable type of contractual arrangement has been used, and whilst we can all point to examples of each having produced satisfactory — or at least acceptable — results, the continued search for and application of new contractual approaches (for example, EPC/EPIC) seems a clear indication that none has been consistently successful.[11]

There is no doubt that the search for the best project delivery strategy for any particular project necessitates a review of many options, which include:

- "traditional" construction contracts
- "improved" construction contacts
- design and construct contracts
- document and construct contracts
- novated design and construct contracts
- EPC (Engineer Procure and Construct)
- EPCM (Engineer Procure and Construction Management)
- EPIC
- BOO (Build Own Operate)
- BOOT (Build Own Operate Transfer)
- construction management contracts
- project management contracts
- partnering
- project alliancing.

[9] Wilson, *Partnering & Alliancing: The Contractor's Viewpoint* (April 1994).
[10] *Cost Reduction Initiative for the New Era* (1994).
[11] Scott, op cit n 5, p 4.

By way of example of industry trends, "improved" construction contracts, partnering and project alliancing will be considered.

Improved construction contracts

Notwithstanding the contribution to the construction industry by CIDA until its demise on 30 June 1995, and now by the Construction Industry Council, it is fair to say that the standard construction contracts in Australia are very traditional in their style and content (see, for example, the Second Pre-postal Ballot Draft Revision of AS2124-1992, issued October 1996).

The British have been somewhat more innovative, and the Institution of Civil Engineers has produced, as an alternative to its more traditional ICE 6th Edition, the New Engineering Contract. This contract has received considerable support. The Latham Report[12] describes the approach of the New Engineering Contract as extremely attractive, and makes a number of recommendations as to contract conditions, only a few of which are incorporated into the standard Australian construction documents. Those recommendations are:

(a) a specific duty for all parties to deal fairly with each other, and with their subcontractors, specialists and suppliers, in an atmosphere of mutual co-operation;

(b) firm duties of teamwork, with shared financial motivation to pursue those objectives (should involve a general presumption to achieve "win-win" solutions to problems which may arise during the course of the project);

(c) a wholly interrelated package of documents which clearly defines the roles and duties of all involved, and which is suitable for all types of project and for any procurement route;

(d) easily comprehensible language, with guidance notes attached;

(e) separation of the roles of contract administrator, project or lead manager and adjudicator (project or lead manager should be clearly defined as the client's representative);

(f) a choice of allocation of risks, to be decided as appropriate to each project but then allocated to the party best able to manage, estimate and carry the risk;

(g) taking all reasonable steps to avoid changes to pre-planned works information; (Where variations do occur, they should be priced in advance, with provision for independent adjudication if agreement cannot be reached.)

(h) express provision for assessing interim payments by methods other than monthly valuation; that is, milestones, activity schedules or payment schedules; (Such arrangements must also be reflected in the related subcontract documentation. The eventual aim should be to phase out the traditional system of monthly measurement or remeasurement, but meanwhile provision should still be made for it.)

[12] Sir Michael Latham, *Constructing the Team* (July 1994), para 5.17(5).

(i) clearly setting out the period within which interim payments must be made to all participants in the process, failing which they will have an automatic right to compensation, involving payment of interest at a sufficiently heavy rate to deter slow payment;
(j) providing for secure trust fund routes of payment;
(k) while taking all possible steps to avoid conflict on site, providing for speedy dispute resolution, if any conflict arises, by a pre-determined impartial adjudicator/referee/expert;
(l) providing for incentives for exceptional performance; and
(m) making provision where appropriate for advance mobilisation payments (if necessary, bonded) to contractors and subcontractors, including in respect of off-site prefabricated materials provided by part of the construction team.

The NEDC Report *Partnering in the Public Sector*[13] also suggests that the New Engineering Contract has much to commend it.

The underlying philosophy of the New Engineering Contract is to encourage efficient and effective project management on construction contracts, and it particularly encourages trust and effective communication between the parties. The style is plain English and it is markedly different to the standard Australian forms.

Partnering

Charles Cowan describes partnering as being:

> "about going back to the way people used to do business, and putting the handshake back into business. Partnering empowers those involved in the project with the freedom and authority to accept responsibility to do their jobs by encouraging decision-making and problem solving at the lowest possible level of authority. It encourages everyone to take pride in their work and tells them its OK to get along with each other.
>
> Partnering provides a mechanism for co-operation between the participants to occur, so that energy-sapping disputation is removed, and productive working relationships are carefully and deliberately built based on mutual respect, trust and integrity."

As one leading figure in the construction industry in Australia has observed:[14]

> "If partnering is doing business the old-fashioned way, with a handshake and smile founded in mutual trust, respect and sharing of objectives, then it is a concept as old as Methuselah. What is new, and exciting, is that this concept is being applied to what some observers might say has been the last bastion of the knucklemen — the

[13] (October 1992).
[14] Duff, "Current Practices in Strategic Partnerships" (1994) 53 AJPA 29 at 30-31.

> construction industry — where conflict has been for such a long time accepted as a normal, and indeed even perversely comfortable, element in our way of doing business."

Partnering is an imported product, as is project alliancing. Partnering was imported from the United States, where it was championed by Charles Cowan of (at that time) the United States Corps of Engineers. Project alliancing, on the other hand, was imported from the North Sea, where it was championed by, amongst others, BP.

As a general rule, partnering exists in parallel with a traditional construction contract. Prior to or shortly after execution of the contract, a workshop (typically of two days' duration) is held, attended by all levels of the project team of both the principal and the contractor. The outworkings of that workshop are encapsulated in a "partnering charter", signed by all those attending the workshop. The parties identify key concerns and determine how problems can be addressed at the earliest opportunity and resolved at the lowest level. A process for ongoing implementation is agreed to ensure that partnering concepts are adopted throughout the life of the project. The partnering charter and the detailed outworkings of the workshop are usually expressed to be of a non-legally binding nature. In effect, the parties are saying to each other that they will act reasonably and fairly and shake hands on it, while expressly disavowing any legal obligation to act fairly and reasonably. To a cynic, it is a little like saying: "Trust me, I'm a lawyer!"

Duff is correct in saying that:

> "the key elements of partnering have to be understood and applied with vigour and honesty if partnering is to work as it should, rather than being a cynical exercise in lip-service to yet another buzz word that will be the salvation of the construction industry.
>
> Those key elements are ... Commitment ... Equity ... Trust ... Development of mutual goals ... Implementation ... Continuous evaluation ... and Timely responsiveness."[15]

The number one element must be commitment. There is no room for tokenism or lip-service in the implementation of partnering; it has to be total commitment from the top down by all parties.

Project alliancing

Of all the new approaches to the delivery of construction projects, project alliancing is the most innovative and it challenges many attitudes and practices which have long been entrenched in the industry. What is project alliancing? Project alliancing is characterised by the following:

1. It is a novel contractual arrangement.
2. It applies the best resources of each participant.
3. It emphasises working together efficiently.
4. It eradicates contingencies.
5. It focuses on project results, not "claimsmanship".

The remainder of this paper deals with project alliancing in more detail.

[15] Ibid at 31-32.

UNDERSTANDING PROJECT ALLIANCES

History of project alliancing

In the 1980s, the emphasis in the construction industry was in the area of quality. In the early 1980s it was Quality Assurance, and then in the late 1980s it was Total Quality Management.

The emphasis in the 1990s shifted to focus on project delivery strategies. An area consistently identified as requiring attention was the need for the parties involved in delivering a project to work in a non-adversarial manner. Different models evolved in the United Kingdom and the United States to achieve this objective. In the United States the "partnering" model evolved, and in the United Kingdom it was the "project alliancing" model.

BP[16]

In the early 1990s BP recognised that it needed project delivery strategies which would result in sustainable lower costs. It undertook a radical examination of all practices and attitudes and realised that an organisation had been built up which, whilst undoubtedly capable of achieving technical excellence, for the most part held contractors and suppliers in relatively low esteem. The overwhelming attitude was that BP knew best and that it could not rely on contractors and suppliers to deliver unless it finely detailed its requirements and then employed large teams to monitor, check and police at every stage. It was clear to BP that these attitudes and practices were a root cause of high costs and that taking action to change them was a prerequisite to achieving its goals.

It was clear that, whilst there was no single panacea for the industry's ills, changes in behaviour and relationships by and between all parties would be critical to future success.

Initially, BP applied the concepts of partnering on an existing operating field. It felt that the results achieved were sufficiently successful to encourage further development. From those experiences, however, BP formed the conclusion that something more was required, particularly in relation to "greenfield" developments, characterised by the involvement of a large number of contractors and suppliers. BP felt that attempting directly to introduce "partnering" across the board with so many companies of diverse natures, interests and attitudes, would significantly lessen the chances of a successful outcome.

The approach which evolved was that of project alliancing.

BP initially set up two project alliances; namely the Hyde Project (an alliance comprising BP, Statoil, the designer (Kvaerner H&G) and the fabricator (UIE)) and the Andrew Project (an alliance comprising the field operator (BP), design, procurement and management services (Brown &

[16] See generally, Scott, op cit n 5, esp pp 2 and 4.

Root), jacket construction (Highland Fabricators), integrated deck construction (Trafalgar House), accommodation module design and construction (Emtunga), transport and installation (Saipem), drilling design and construction (Santa Fe), and pipeline construction and installation (Allseas). BP was very pleased with the outcomes from these alliances. The Hyde project was completed some 25 per cent below the agreed target.

Ampolex[17]

The first project alliance in Australia was the *Wandoo Project*. The alliance consists of the operator (Ampolex); the designer of the concrete gravity structure and casting basin at Bunbury (Ove Arup and Partners); the constructor of the concrete gravity structure and casting basin (Leighton); the designer of the offshore pipeline, with responsibility also for offshore installation, hookup and commissioning (Brown and Root); and the designer of the accommodation facility and fabricator of the steel topsides (Keppel).

In March 1994, two of Ampolex's general managers travelled to the United Kingdom to visit contractors and clients with first-hand experience with alliancing. The impressions gained by those managers during their visit were:

1. The alliance teams visited were "super" enthusiastic, particularly from the clients' side.
2. Organisations were projecting prior to project completion extraordinary savings in cost and time from the alliancing process.
3. The client/contractor staff integration was seamless.
4. The traditional walls between client, designer, fabricator and installation contractor were being broken down, opening up the possibility of significant improvement in project management efficiencies and therefore cost and schedule savings.
5. Reduction in project management cost of projects was evident, due to the elimination of man-marking between client/contractor as a result of integrated teams.
6. The alliance must operate as a separate single entity outside the operating regimes of client and all participants. To be successful the alliance had to be a separate entity with its own identity and be supported by the client and all participants.

Following this visit, Ampolex committed, in April 1994, to use a project alliance to develop the Wandoo oil field for the following reasons:

1. There was a high probability that development costs could be reduced through alliancing.
2. The alliance offered the potential to share the schedule and cost risk of developing Wandoo. This was a significant issue as Ampolex had 100 per cent equity in the field at that time.
3. Ampolex had to get it right the first time. Alliancing offered the possibility of learning from the major oil companies by using internationally experienced oil and gas organisations.

[17] See generally, Minns and Kava, "Alliancing and the Wandoo Project", paper presented to Offshore Australia (incorporating Petrochem 95 conference), 22-24 November 1995.

4. Client companies in the North Sea were carrying out large projects with minimum staff and management teams through alliancing. This approach suited the Ampolex corporate organisational philosophy.

At the time of writing the Wandoo Alliance has been operating for nearly two years. Given that first oil is still a few months away, Ampolex believes it premature to comment on whether the project has been a success. However, Ampolex believes that those involved would agree that the process has been positive. It is particularly pleased with the smooth integration of its own staff and personnel from the various alliance participants, and that as a general rule the players have conducted themselves in accordance with the agreed principles. The classic example provided by Ampolex is what they refer to as the "now famous 'bund wall failure'". In April 1995 the bund wall in the Bunbury Casting Basin failed and the basin flooded. This caused some disruption to the planned schedule but, consistent with the "no blame" principle, the parties focused on fixing the problem with the minimum impact on cost and schedule.

WMC[18]

In mid-1994, WMC determined to use a project alliance for development of the East Spar Project. Hence, hot on the heels of Ampolex, representatives from WMC, Kvaerner and Clough (the East Spar Project alliance participants) visited the United Kingdom to meet with United Kingdom operators and contractors to learn from their alliancing experience, and found the visit very positive.

WMC believes that the alliance arrangement has been successful in providing the flexibility to develop new facilities concepts whilst maintaining project cost and schedule objectives. It has also found that the ability to incorporate new technologies and new combinations of technologies without the impediments of traditional client-contractor relationships to be a benefit of alliancing.

Further, feedback from the East Spar project team has been positive, particularly with respect to working in a co-operative environment with common goals as opposed to a traditional "conflict" environment. WMC believes that a successful result on East Spar and other alliances will provide industry confidence in this concept as an attractive contracting strategy for future projects.

BHP

BHP Direct Reduced Iron has decided to project alliance both the construction work and the provision of fabricated steel on its massive DRI project at Port Hedland. The construction alliance is unusual in that major elements of the work, such as design and equipment supply, are excluded from the alliance. Both alliances are up and running and the initial feedback is positive. However, it is early days yet on this project.

[18] See generally, Campbell and Minns, op cit n 7.

Principles of project alliancing

First and foremost, it must be remembered that project alliancing is strictly a business relationship. This relationship is built on the following principles:[19]

(a) a primary emphasis on the business outcomes from all parties (that is, win-win);
(b) clear understanding of individual and collective responsibilities and accountabilities;
(c) an equitable balance of risk and reward for the parties;
(d) encouragement of openness and co-operation between the parties;
(e) encouragement to develop and apply innovative approaches and achieve continuous improvement;
(f) access to and contribution by the expertise and skills of the parties; and
(g) a commercial basis which offers the opportunity to achieve rewards commensurate with exceptional performance.

If ranking is appropriate, alliancing is, first, about people. It is establishing a team of the best people for each job, drawn from each participant's organisation. It is the successful integration and motivation of this team which will determine the success or failure of the alliance.

Secondly, it is particularly important that the proper commercial drivers be agreed upon. A major feature of alliancing which has to be appreciated at the outset is that, as a general rule, the operator pays all of the direct costs and overheads of the other alliance participants, even if the work is carried out negligently. The gain (or pain) is determined by the overall success of the project measured against key performance indicators, and it is in that way that each of the participants is affected by, for example, the final cost of the project. Extraordinary results give rise to extraordinary returns.

Finally, there is the contract documentation, the purpose of which is to give effect to the above. If, however, this documentation is being read and quoted in a pedantic fashion, then it is suggested that the alliance is in real difficulty, as the spirit of alliancing should prevail over a legalistic interpretation. That has certainly been the general experience on alliances to date.

Contractual structures of project alliances

As will be seen, while the key principles are common, there is not a rigid formula for the contractual structure of a project alliance. The actual structure adopted is influenced by the nature of the project and the culture and corporate objectives and drivers of each of the alliance participants. To date, there are three main contractual models for an alliance: the two-contract model, the multiple-contract model and the single-contract model. It is emphasised, however, that as a question of practical day-to-day operation, the alliances work in exactly the same fashion, whichever option is selected. The key objective of

[19] Scott, op cit n 5, p 5.

an alliance is to have the parties work together in an enthusiastic and positive manner, whatever nature of obstacle may arise during the course of the project. Each of these three contractual models achieve that, and the essential integrated nature of alliancing is the same in each of the models.

Option 1: the two-contract model

This contractual arrangement (see Figures 2 and 3) was used on the Hyde and East Spar projects.

The first contract is the alliance agreement. This agreement establishes the project delivery vehicle (that is, the alliance). It covers the matters referred to below under the heading "The alliance agreement".

Figure 2: East Spar alliance agreement

The second contract is the development contract. This agreement deals primarily with the works which the project delivery vehicle must deliver. It is in many ways a fairly traditional development/construction contract, and covers the matters referred to below under the heading "The development contract". A very interesting feature, however, is that the operator appears on both side of the development contract, a feature which is made even more interesting (at least from a lawyer's viewpoint!) if the obligations of the alliance participants are joint and several.

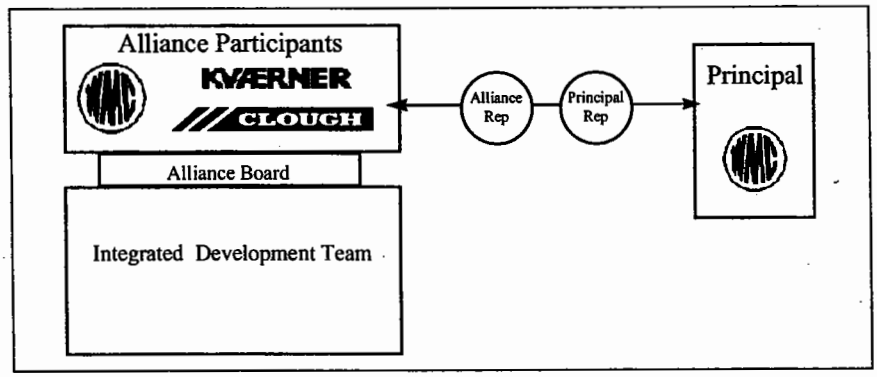

Figure 3: East Spar development contract

Option 2: the multiple-contract model

This contractual arrangement (see Figures 4 and 5) was used on the Andrew and Wandoo projects.

The first contract is the alliance agreement. This agreement is essentially the same as that in option 1, above.

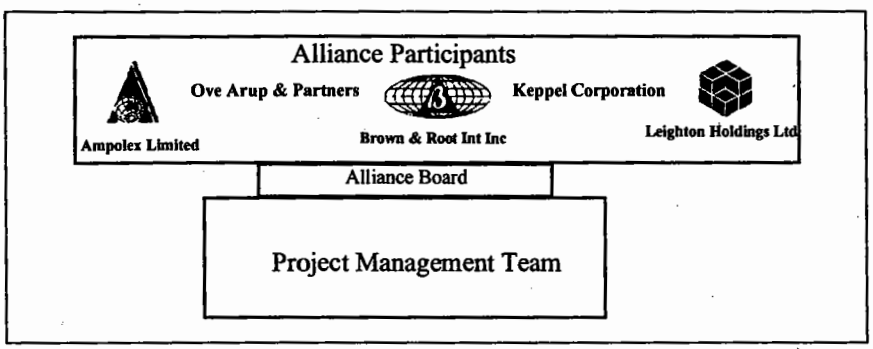

Figure 4: Wandoo alliance agreement

The reason for the multiple contracts is that, instead of a single development/construction contract, the operator enters into individual development/construction contracts with each of the other alliance participants. As for option 1, however, the contracts are fairly traditional and cover the same matters as in option 1.

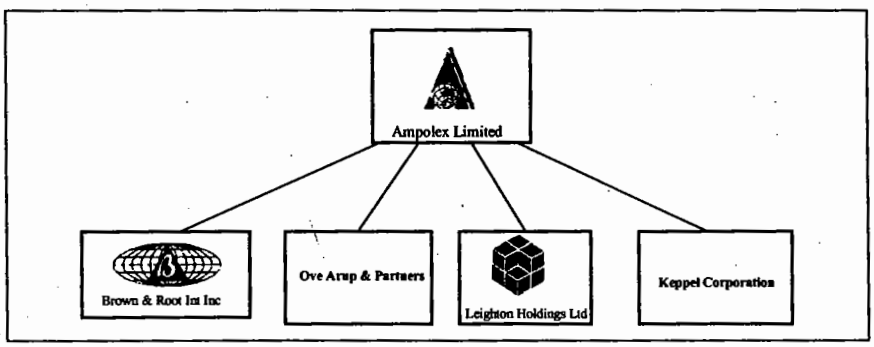

Figure 5: Wandoo development contracts

Option 3: the single-contract model

This contractual arrangement (see Figure 6) has been adopted by BHP on both the construction and fabricated steel alliances on its massive Port Hedland project. In essence, it is option 1, but with the two contracts rolled into a single contract. The first part of the contract deals with the matters contained in the alliance agreements under options 1 and 2, while the latter part of the contract deals with the matters covered in the option 1 and 2 development/construction contracts.

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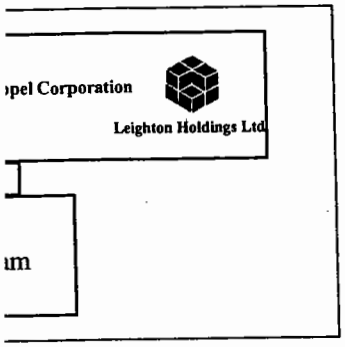

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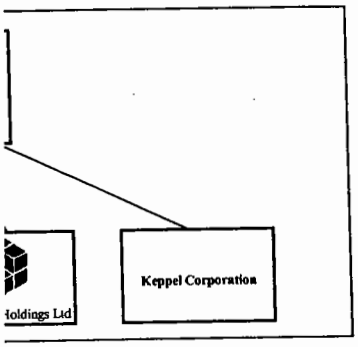

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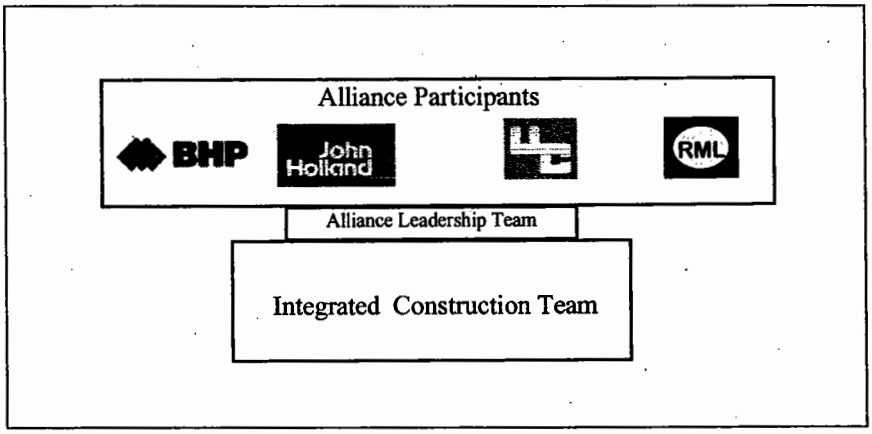

Figure 6: Port Hedland Construction Alliance unified alliance and construction contract

The alliance agreement

Whichever option is adopted for a particular alliance, the following are the key principles relating to the contractual terms establishing the alliance. In general, an alliance agreement:

(a) establishes a new and novel project delivery vehicle;
(b) encourages the parties to co-operate for mutual benefit;
(c) sets out the mission statement and the objectives of the parties;
(d) establishes an alliance board and an integrated development team;
(e) sets out the commercial arrangements as between the parties;
(f) emphasises innovation and internal resolution of conflict; and
(g) introduces the concept of "no dispute".

There are a number of points to consider in relation to an alliance agreement, including:

(a) establishing the alliance board:
  (i) composition (representatives from each participant);
  (ii) voting (equal voting rights); and
  (iii) unanimity (it is recommended that unanimity be required and that no mechanism be included to deal with a deadlock; the board should be left to resolve the matter).
(b) establishing the integrated development team:
  (i) drawing upon the best available resources of each of the participants to fill each position. The integrated team is distinct from the organisations of each of the participants. It is housed in separate offices and operates with its own logo and identity et cetera, in order to create an appropriate environment for working together to achieve common goals; and
  (ii) management structure.

(c) establishing the commercial arrangements between the parties:
  (i) "no dispute";
  (ii) splitting the margin (value of works?; ability to influence?);
  (iii) personal injury, property damage and third party liabilities;
  (iv) joint and/or several liability;
  (v) liability limitation;
  (vi) "default" of a party; and
  (vii) dispute resolution.

The development contract(s)

Again, whichever option is adopted for a particular alliance, the following are the key features of the contractual terms which govern the work which the alliance participants have to carry out:

1. In general, the development contract(s) are a relatively conventional form of development/construction contract. (BP use as a base their standards works contract, as did Ampolex and WMC, in each case modifying the contract to reflect the alliancing principles. The Port Hedland project alliance participants were particularly keen that the single document be drafted in the spirit of alliancing, and hence BHP has significantly altered the drafting style of its standard document, while retaining its key requirements.)
2. The development contract sets out the commercial, technical and performance criteria for the delivery of the project by the Alliance.
3. The development contract sets out "no dispute".

It is worth elaborating upon "no dispute". One of the inherent features of alliancing is that the parties are not looking over their shoulders, so to speak. "Blame" is contrary to the fundamental concept of alliancing, and hence the associated contracts restrict access to the courts to breaches of contract or duty which amount to a "wilful default". Hence, the parties do not sue each other over questions of negligence, or even gross negligence. Only in the event of "wilful default" do the parties have a cause of action against each other and, assuming that appropriate commercial arrangements accompany the alliance, it is difficult to see "wilful default" arising except in the event of insolvency.

There are a number of points to consider in relation to a development/construction contract, including:

- defining direct costs
- agreeing overheads
- agreeing forecast cost
- agreeing risk/reward regime
- agreeing key performance indicators
- audit provisions (open-book nature of alliancing)
- consequential loss: limitation of liability
- "no dispute"

- design (especially state of completion)
- variations
- extensions of time
- force majeure
- remedial work and defects liability
- insurances and indemnities
- dispute resolution
- termination.

See Figure 7 for a contractual checklist for alliance documentation.

- How many contracts?
- Joint and/or several liability
- Separate legal entity for the alliance?
- Alliance purpose: scope of business, statement of requirements, clarity of outcomes
- Alliance lifespan: project studies through to operational status
- Balance of requirements: Capex, time, plant performance and reliability, whole-of-life costs
- Flexibility of alliance to add/delete parties
- Interaction and involvement of existing operations
- Alliance organisation structure: board representation of parties, team roles
- Roles/responsibilities of each key position/team
- Define management approach: leadership style, shared vision. enrolment of all parties
- Project target costs development process: accuracy, confidence level, robustness
- Definition of cost structure
- Risk/reward-sharing basis: overall capital and influence contribution
- Method of profit distribution
- Handling of variations: change of intent only
- Handling of escalation, Forex
- Audit function: extent, process
- Standards of workmanship
- Contract documents: method of development, time, level of prescriptiveness
- Contractual authority of the alliance and parties thereto
- Guarantees by the parties
- Securities: extent, value
- Indemnities and liabilities of the parties to the alliance, consequential loss, etc
- Insurances regime
- Sub-alliancing, subcontracting etc
- Remedial work

Figure 7: Contractual checklist

The commercial drivers

It is particularly important that the best commercial drivers are put in place in the alliance documentation. Each of the participants will have different factors motivating them, and it is worth spending considerable time ensuring that the right motivators have been identified and that realistic targets (albeit stretch targets) are agreed. For example, when the forecast cost is being agreed, it is important that contingencies are identified and removed. The shape of the risk/reward curve is the most appropriate mechanism for dealing with estimating uncertainty.

Another very important question is the extent of "pain" which is appropriate for the alliance participants if the project does not perform to expectations. The structure of the Wandoo project, for example, had the alliance participants put all of their "normal" profit and recovery of their corporate overheads at risk.[20]

It is wise to structure the commercial arrangements so that they require minimal adjustment during the course of the works. There should be only very limited grounds for adjustment of the risk/reward regime. Grounds for extensions of time and shifting of the forecast cost should be very narrow, as the parties should be focused on performance and not on reasons for non-performance.

To date the risk/reward regimes have always dealt with the final cost and time of completion, with the margins determined on how well the final performance compared with the planned performance. Some alliances, however, have also allocated significant risk/reward on performance in areas such as safety and environmental performance.

Figure 8 is an example of risk/reward based upon actual costs of the project.

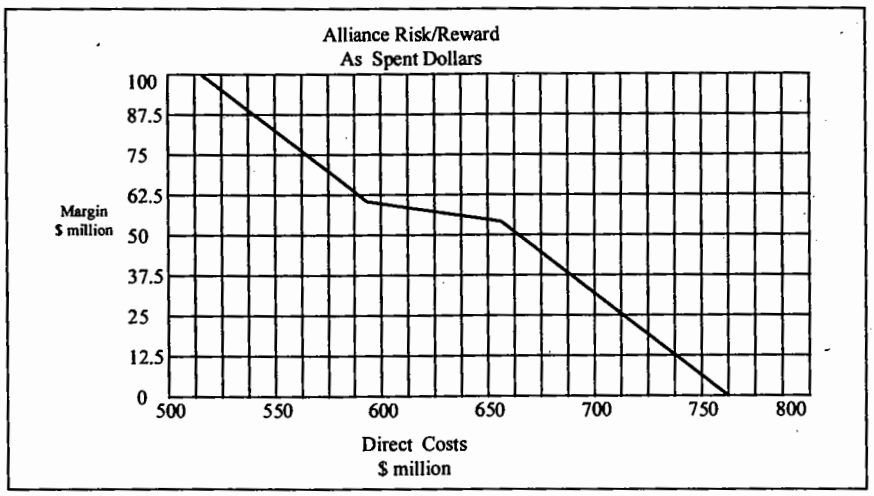

Figure 8: Risk reward curve

[20] Campbell and Minns, op cit n 7.

Sub-alliancing/subcontracts

An issue in relation to subcontracting and sub-alliancing is the legal nature of the alliance. For example, on the East Spar project, WMC entered into each subcontract as agent for the alliance participants; whereas on the Wandoo project, a new Ampolex subsidiary called Wandoo Alliance Pty Ltd was incorporated to be the public face of the project management team and the Wandoo alliance as a whole. The board of directors of WAPL has the same composition as the alliance board.[21]

As experience with alliancing grows, more innovative steps should be considered in the area of works carried out by non-alliance participants.

Such steps may include ramping companies in and out of the main alliance for a period of time, forming sub-alliances and partnering arrangements and so on. This is a largely untapped area, but it is clearly important given the impact such parties will have upon the overall success of the project. For alliancing to truly succeed, its spirit ought to be passed as far down the contractual chain as possible.

The bit players

The lawyers [22]

Alliancing actually requires a different attitude from the lawyers. A good alliancing lawyer is very much in a facilitator role. The lawyer has to have an inherent understanding of alliance principles, understand the wishes of each participant, facilitate consensus and then promptly implement what are quite often innovative ideas. The initial reaction of many lawyers to alliancing is cynical and/or negative, which is unfortunate.

A United States commentator[23] notes that lawyers retained to assist in the development of alliance agreements may find their role quite different from that performed in more traditional contract relationships. She notes that, while the positive results in partnering are in large measure tied directly to the participants' level of sophistication and commitment, lawyers sensitive to the special needs of this type of relationship can substantially enhance the potential for a successful alliance in its early stages.

The facilitators

Alliancing requires a huge and sudden change in the way in which project work is executed and in the way the participants deal with each other. Some people do not react well to change. Or, as one chief executive put it in relation to the change that goes with alliancing:[24]

[21] Ibid.

[22] Duff, op cit n 14, at 31, notes that he "was hugely heartened by an article in the American industry journal *Equipment World* (1991), which had a short but perceptive editorial on partnering. The title of the editorial said it all: 'Partnering: One Way to Starve Your Lawyer'."

[23] Kunz, "Counsel's Role in Negotiating a Successful Construction Partnering Agreement" in *The Construction Lawyer* (November 1995), p 19.

[24] Pollock, "Partners in Productivity: CEO's must be Champions of Change" (1994) 53 AJPA 14.

> "Generally speaking, people hate change. Many hate it with a passion. Some fight it to the death ... Most human beings feel comfortable with the status quo. They loathe disruption. They resent the applecart being upset. Those of us who run major corporations cannot afford that luxury. We cannot run our businesses tomorrow in the same way that we are running them today. Increasingly, those of us who want to prosper in global markets or even national markets are realising that maybe, just maybe, we cannot do it all by ourselves. To compete and prosper, we must become smarter. We have got to do things differently. We must accept that change is inevitable and we must not be frightened by that reality. To a large extent, we have got to accept that, in a corporate world, tradition is poison."

Facilitators are very useful for implementation of the required changes. Indeed, in the United States, one major insurer of design professionals, and strong advocate of partnering, believes a professional facilitator is so advantageous that it has offered to pay for the costs of a partnering facilitator on large construction projects.[25]

CONCLUSION

Alliancing to date has been adopted primarily on large-scale projects and with "blue-chip" companies as the alliance participants. These companies have all had many, many years of experience with various forms of contracting strategies, and certainly have their own "in-house" traditional contracts

They have each, however, formed the view that for certain major projects, alliancing is the appropriate contracting strategy. The first projects have come in successfully and the feedback from those currently in hand is very positive.

Alliancing is not a panacea, but is certainly making its mark in major project work. Continued good results from alliancing will ensure its future as a desirable project delivery strategy for major projects.

[25] "Insurer to Pay Cost of 'Partnering' Facilitator: DPIC Companies, Inc" (1994) 25 (No 2) *Building Design & Construction* 7.