

### **WATERTIGHT STEP-IN RIGHTS**

#### **MP WATER PTY LTD IN ITS CAPACITY AS TRUSTEE FOR THE MP WATER TRUST V VEOLIA WATER AUSTRALIA PTY LTD [2022] NSWCA 127**

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### **INTRODUCTION**

In *MP Water Pty Ltd in its capacity as Trustee for the MP Water Trust v Veolia Water Australia Pty Ltd* [2022] NSWCA 127, the Court of Appeal (Mitchelmore JA) considered two issues which arose in the context of the issuance of 'step-in notice' by a project company to a service provider under a service provider agreement ('SPA') following a major service failure.

The first ground of appeal was about the obligation of a service provider to 'assist' following the issuing of a step-in notice and the second was the respondent's contention that the facility had not come into existence under the terms of the project documents, by the date of the Major Service Failure. Without a certified facility, the respondent contended there could be no Major Service Failure and consequently no default of provisions to remedy any such Major Service Failure.

Mitchelmore JA (with whom Ward P and Macfarlan JA agreed), allowed the appeal and made the declaration sought by the appellant. Her Honour held that the valid issuance by the project company of a 'step-in notice' authorised the project company to give directions to the service provider to 'assist' in the assumption of total or partial possession, management and control of the facility (or any part of the facility) and the provision of the services by the project company.

Rejecting the respondent's notice of contention, Mitchelmore JA upheld the primary judge's finding that the definitions proposed by the respondent for 'facility' would if accepted, subvert the regime in the SPA dealing with the commencement of obligations under the SPA. Further the respondent's interpretation would necessitate that nine different actions would have to occur for

each and every element of the facility for the definition of Major Services Failure to be engaged. This is not an understanding which a reasonable business person would hold and would be inconsistent with the commercial purpose of the SPA and its safety objects.

### **BACKGROUND**

MP Water Pty Ltd (MP Water) is a special purpose project company created to build, operate and maintain a water treatment facility (facility) for a joint venture customer conducting underground coal mining operations at the Springvale and Angus Place Mines in the western coalfields of New South Wales.

MP Water entered into a water treatment services contract ('WTSC') with the customer and further project documents with Veolia Australia Pty Ltd (Veolia) including a design and construct contract and service provider agreement ('SPA'). Pursuant to the SPA, Veolia would operate and maintain the facility. The mining operations generate approximately 25 megalitres of water each day, irrespective of the activities being conducted. The facility is required to enable water to be extracted continuously to:

- (a) avoid the saturation of the strata and to prevent any damage to the integrity of the underground tunnels in the mine; and
- (b) to provide for the cooling circuits at the nearby Mt Piper Power Station.

Veolia contracted to guarantee capacity to process specified volumes of mine water. In the event that the volumes exceeded the guaranteed capacity, Veolia had a right under the SPA to recover an additional charge for that water but had no right to refuse to take the additional volumes. The SPA contemplates that Veolia is responsible for maintaining 'buffer

ponds' should a disruptive event occur preventing Veolia from accepting and processing all mine water through the facility.

If, for a continuous period of 48 hours, the facility fails or ceases to be able to accept mine water to the guaranteed capacity, a Major Service Failure occurs. This event enables MP Water to issue a Service Provider Default Notice calling on Veolia to remedy the failure within an applicable cure period. Where the failure has not been cured within specified periods, a default termination event arises, triggering the step-in rights of MP Water.

Clause 44 of the SPA provided:<sup>1</sup>

*(a) If at any time during the Operations Phase:*

*(1) a Services Provider Default Termination Event occurs;*

*(2) a Services Provider Default occurs and the Services Provider has failed to diligently pursue the relevant Services Provider Default Notice; or*

*(3) it is necessary for Project Co to take immediate action to discharge its statutory duties or powers, or comply with its obligations under applicable Laws and Approvals,*

*(4) a 'Project Co Default Termination Event' occurs under and as defined in the WTSC;*

*(5) a 'Project Co Default' occurs under and as defined in the WTSC and Project Co has failed to diligently pursue the relevant 'Project Co Default Notice' under and as defined in the WTSC; or*

*(6) it is necessary for the Customer to take immediate action to discharge its statutory duties or powers, or comply with its obligations under applicable Laws and Approvals,*

Project Co (paragraphs (1) to (3)) or the customer (paragraphs (4) to (6) and in accordance with clause 44 of the WTSC) may elect, and if it

so elects the Services Provider will assist Project Co or the customer wherever and however possible to ensure that Project Co or the customer is able, to:

*(7) temporarily take or assume total or partial possession, management and control of the Facility (or any part of the Facility) and the provision of the Services (or any of them);*

*(8) take such other steps as are necessary or desirable to continue the provision of the Services as required by this Contract or to minimise the risk to the Environment, to other members of the general public or of material damage to the Facility, as applicable; and*

*(9) do anything which the Services Provider is entitled to do under an O&M Project Contract or with respect to the Project.*

*(each a Step-in Right)*

## **THE STEP-IN EVENT**

In late April, early May of 2021, water from the mine had flowed into one of the buffer ponds at a volume which exceeded the maximum level permitted. Veolia requested that MP Water stop or reduce the flow of mine water to prevent overflow or spillage from the pond into the environment. MP Water gave notice to the customer to stop the mine water flow. The customer stopped the flow of mine water.

After a period of more than 48 continuous hours of the facility failing or ceasing to accept the mine water, the customer issued a default notice to MP Water<sup>2</sup> contending that there had been a Major Service Failure under the WTSC, that MP Water was in default under the WTSC and requiring MP Water to remedy the default by restoring the facility's ability to receive mine water to the guaranteed capacity by 5pm that day.<sup>3</sup>

The issue of the step-in notice manifested an election by MP Water to take or assume partial possession, management and control of the facility and the services. By this election, Veolia did not remain in possession and control of the whole facility and the assistance obligation was triggered.

MP Water issued notices of default and direction to Veolia (which were disputed) and ultimately issued a 'step-in notice'.<sup>4</sup> Veolia rejected the step-in notice as unlawful and MP Water sought injunctive relief.<sup>5</sup> Injunctive relief was granted on 20 May 2021. By August 2021, the effect of the Major Service Failure had been overcome.

### **AT FIRST INSTANCE<sup>6</sup>**

Proceedings were commenced by MP Water in the New South Wales Supreme Court to determine whether Veolia's failure to accept and process the mine water was a breach of the SPA.

At first instance, Williams J found that the step-in provisions had been engaged by Veolia's failure to comply with the service provider default notices.

The issue between the parties was summarised as:<sup>7</sup>

*... whether Veolia's obligation in clause 44(a) to 'assist' MP Water where MP Water elects to step in requires Veolia to comply with instructions or directions issued by MP Water specifying the steps to be taken by Veolia in providing the services or overcoming the effects of a Services Provider Default.*

Williams J considered the step-in rights of MP Water to be cumulative rather than separate rights.

In the context, the primary judge held that:<sup>8</sup>

*... sub-clause 44(a)(7) does not require Veolia to assist MP Water to take total or partial management of some or all Services (by issuing directions or instructions or instructions to Veolia) whilst Veolia remains in possession and control of the whole of the facility and performs the services under MP Water's instructions.*

The primary judge's finding was that the step-in rights in clause 44 of the SPA provided MP Water with 'a different right to step in and

take total or partial possession, management and control in each of the circumstances referred to in clause 44(a)(1) to (3), and to require Veolia to step aside'.<sup>9</sup> The primary judge's reasoning would necessitate an application to the court for injunctive relief should MP Water seek to direct Veolia to do or refrain from doing specific things.<sup>10</sup>

Veolia submitted that the step-in notice was invalid because at the time of the Major Service Failure, the facility as defined in the SPA did not exist. This contention was based on the fact that the definition of facility included a mine water buffer pond which had not been repurposed, commissioned and tested by Veolia.

The primary judge rejected Veolia's contention, which amounted to an assertion by Veolia that the Service Commencement Date had not occurred<sup>11</sup> and also found that a reasonable business person would not have understood that the definition of Major Service Failure could only be engaged once each and every element of the facility 'had been designed, engineered, procured, supplied, constructed, tested and commissioned and was being operated and maintained in accordance with the WTSC'.<sup>12</sup>

### **ON APPEAL**

The appeal joined issue with the primary judge's findings on the ability of MP Water to direct Veolia to take certain actions to overcome the service provider default once a step-in notice had been issued.

By notice of contention, Veolia submitted that the primary judge erred in not dismissing MP Water's claim on the basis that the facility had not come into existence at the date of the Major Service Failure in May 2021. Without the existence of the facility, no Major Service Failure could have occurred and Veolia could not be in default in failing to treat the mine water to the guaranteed capacity.<sup>13</sup>

### **CONSTRUCTION OF THE STEP-IN RIGHTS**

Applying the principles which govern the construction of commercial contracts,<sup>14</sup> her Honour accepted that:

*... the election that clause 44 confers on MP Water and the customer is for a remedial purpose. Paragraphs (7), (8), and (9) collectively constitute the actions which MP Water (and the customer) may elect to take if one or more of paragraphs (1) to (3), or (4) to (6), occurs. It is inherent in the use of the phrase 'may elect' that MP Water may exercise some, or all, or none, of the actions so conferred*

This being the case, under clause 44 of the SPA, upon the exercise of the right to give such directions, a correlative obligation was imposed on Veolia to 'assist' MP Water, extending to Veolia operating the facility and providing the services at the MP Water's direction.<sup>15</sup>

Mitchelmore JA further rejected as a 'false dichotomy' the primary judge's reasoning that Veolia was not required to assist MP Water to take total or partial management of all or part of the services 'whilst Veolia remains in possession and control of the whole facility and performs the services under MP Water's instructions'.<sup>16</sup>

The issue of the step-in notice manifested an election by MP Water to take or assume partial possession, management and control of the facility and the services. By this election, Veolia did not remain in possession and control of the whole facility and the assistance obligation was triggered.<sup>17</sup>

### **THE EXISTENCE OF THE FACILITY**

Mitchelmore JA held that the primary judge was correct to reject Veolia's arguments about the definition of facility. Acceptance of the contentions would subvert

the regime in the SPA in dealing with the acceptance and commencement of the facility and services.

The fact that the definition of facility used the future tense means it:

*‘...does not need to be read, and should not be read, as requiring each of the component parts to have been ‘designed, engineered, procured, supplied, constructed, tested and commissioned’ and ‘being operated and maintained in accordance with the WTSC’. There is significant force in the primary judge’s reasoning at [252] that this would be unworkable having regard to the many components and parts included within each of the nine elements making up the facility. In particular, before the parties could know whether a failure to accept mine water at the Guaranteed Capacity constituted a Major Service Failure, the parties would first need to satisfy themselves as to whether each and every component of the facility had those features.’<sup>18</sup>*

The more preferable construction was that adopted by the primary judge, which understood the term facility in the definition of Major Service Failure:

*... as descriptive of the facility in the state in which it exists whenever there is a cessation or failure after the Services Commencement Date.*

This interpretation is consistent with the commercial purposes of the SPA and upholds the safety objects its provisions are intended to serve.<sup>19</sup>

## KEY TAKEAWAYS

When drafting step-in provisions:

- Keep the commercial purpose of the SPA and the upholding of safety standards and service availability front of mind. The step-in regime should safeguard these purposes. Project Co or a lender (where dealing with lender direct

agreements) will usually not have the expertise or resources to step-in to service provision.

- Consider and ensure clarity of the regime in the SPA for acceptance of and commencement of services.
- Pay particular heed to separating step-in trigger events from the resultant step-in rights.
- Clearly link the election by a project company to exercise step-in rights with the assistance obligations of the service provider.
- Definitions must work together. Check the interaction of the definitions of commencement or availability of facilities or services with the triggers to default regimes and ultimately, the step-in provisions.

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## REFERENCES

1. *MP Water Pty Ltd in its capacity as Trustee for the MP Water Trust v Veolia Water Australia Pty Ltd* [2022] NSWCA 127 at [31] (*MP Water Pty Ltd in its capacity as Trustee*).
2. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [51].
3. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [54].
4. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [56].
5. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [57].
6. *MP Water Pty Ltd v Veolia Water Australia Pty Ltd (No 3)* [2021] NSWSC 1023 (*Veolia Water*).
7. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [61].
8. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [63].
9. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [65].
10. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [65].
11. *Veolia Water*, n 6, at [250].

12. *Veolia Water*, n 6, at [252].

13. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [102].

14. As summarised by Bathurst CJ in *Lawrence v Ciantar* [2020] NSWCA 89 at [98]–[99].

15. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [97].

16. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [95]–[96].

17. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [96].

18. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [113].

19. *MP Water Pty Ltd in its capacity as Trustee*, n 1, at [114].

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## WHEN IS A CAUSE OF ACTION REALLY 'BASED ON' AN INSURED'S PROVISION OF PROFESSIONAL SERVICES?

**FKP COMMERCIAL DEVELOPMENTS PTY LIMITED V ZURICH AUSTRALIAN INSURANCE LIMITED [2022] FCA 862**

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'The point is that, in the insurance context, a party gets the policy they pay for, not some other policy they could have paid for but (apparently) did not' is one of the concluding remarks in the recent decision of Jagot J.

### INTRODUCTION

This illuminating decision touches on some of the issues that insurers and builders grapple with on a daily basis. A typical claim under a Design and Construct Professional Indemnity ('D&C PI') policy will arise from a claim against a builder and developer under the *Home Building Act 1989* (NSW) ('HBA') and more recently, for alleged duty of care breaches under the *Design and Building Practitioners Act 2020* (NSW) ('DBPA').

D&C PI policies, such as the policy referred to in this case, are intended to provide cover for design, drafting, technical calculation and project management.<sup>1</sup> What are commonly excluded under these policies are the performance of the construction, installation, or physical alteration of buildings, goods, products or property.<sup>2</sup>

This is because these types of policies are not designed to underwrite shoddy construction work.

However, a common occurrence is that insureds will attempt to shoehorn all manner of claims against it to an insurer for cover under a PI policy. What then typically follows is a proverbial game of cat and mouse where an insurer will seek to understand the underlying factual matrix of a claim and whether the insured's liability arose from the provision of professional services under a policy.

The decision of Jagot J (as her Honour then was) in *FKP Commercial Developments Pty Limited v Zurich Australian Insurance Limited* [2022] FCA 862

sheds light on the policy response considerations insurers should be aware of when determining whether a relevant professional indemnity policy responds to a claim under the HBA or DBPA.

### KEY TAKEAWAYS

(1) Not all insuring clauses present in professional indemnity policies will immediately enliven following a claim for civil liability where the claim relates to the insured's provision of professional services.

(2) In order for a claim of civil liability to be 'based on' an insured's provision of professional services, the insured's liability must stem from the provision of 'professional services' as defined under the relevant policy. The mere fact that an insured provided 'professional services' is not enough, a connection is required between the common law cause of action and the professional services provided.

(3) Claims for breach of a statutory duty of care do not prima facie involve the provision of 'professional services'. An insured may seek to characterise these claims as involving or arising from the provision of professional services; however, insurers should be cautious in accepting any explanation at face value and further inquiries must be made as to the elements of the cause of action and the definition of 'professional services' under the policy to determine whether the policy responds to the specific claim made against the insured.

(4) In this matter, while the insured may have been providing professional services under the relevant policy, the statutory and common law causes of action (the 'civil liability') were not based on those professional services, but rather on the statutory liability which may attach due to the status of the insured parties as the owner/ developer and head contractor.