

# MDA PRESENTS



## FIRST AID FOR CONTRACTS



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### UNVEILING THE NOMINATED SUBCONTRACTOR: PERSPECTIVES FROM SOUTH AFRICAN LAW

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**The risk of a mismatch of skill and lack of expertise for a subcontracted part of the works is inevitable in construction projects and often times when Contractors select Subcontractors, they fail to acknowledge and address this risk because of the tight deadlines in the industry or sometimes owing to “just wanting the deal done as soon as possible”. The concept of the Employer nominating a Subcontractor is recognised in most standard form construction contracts and allows the Employer to nominate a specific Subcontractor to carry out specialised works in the project without having to enter into a different contract on the same project.**

#### **JBCC FORM OF CONTRACT**

The JBCC is the only standard form contract among the CIDB-approved Subcontract forms (which include

the JBCC, NEC, FIDIC, and GCC) that specifies that the Employer, through its agent, selects the Subcontractor, negotiates the terms directly with the Subcontractor, and then instructs the Contractor to appoint the Subcontractor on those terms. The Contractor's input is limited to the right to object to the appointment, such as if the Subcontractor refuses to sign the Subcontract agreement or provide security. As a safeguard for the Contractor in this scenario, the JBCC includes clauses that transfer the risk of the nominated Subcontractor's non-performance away from the Contractor.

## **NEC FORM OF CONTRACT**

The NEC contract does not make direct provision for nominated Subcontractors; Subcontractors are proposed by the Contractor for the approval of the Project Manager. The Contractor is required to submit the names of any Subcontractors that they plan to use and have them accepted prior to awarding them any work. It again gives the Project Manager/Employer some control if they have concerns or reasons that they feel a Subcontractor would not deliver in accordance with the scope of work. These could be concerns over quality, safety, or security. It is important to note that if a Contractor elects not to engage with a Subcontractor using an NEC form of contract, they are still required to submit the terms of engagement to the Project Manager for acceptance. This requirement ensures that the Project Manager retains oversight and can review and approve the terms under which the Subcontractor will be engaged, regardless of the specific contract form used.

## **FIDIC FORMS OF CONTRACT**

Clause 5 of the 1999 and 2017 Red book Conditions defines a 'nominated Subcontractor' as either a Subcontractor named in the Contract as being 'nominated' or a Subcontractor whom the Engineer instructs the Contractor to utilize as a Subcontractor under clause 13.

The Contractor may object to the use of a nominated Subcontractor. A number of grounds for objecting are deemed reasonable, including where there are reasonable grounds to believe that the Subcontractor lacks sufficient resources, competence, or financial strength to complete the subcontracted works; or where the Subcontractor refuses to carry out the

works in a manner that ensures the Contractor does not breach its own obligations under the main contract. In the event where the Employer requires the Contractor to use a nominated Subcontractor despite a reasonable objection, the Employer must agree to indemnify the Contractor against the consequences of the matters listed that validate reasonable objection.

There is a particular condition within the FIDIC Red Book that specifies that the Contractor must pay the amounts certified by the Engineer to be due under the Subcontract to the nominated Subcontractor. However, before issuing a Payment Certificate to the Contractor the Engineer may ask for evidence that previous payments have been made to the nominated Subcontractor. If evidence is not provided by the Contractor or the Contractor does not satisfy the Engineer that there are grounds for withholding payment, then the Employer may at its discretion pay the nominated Subcontractor directly. This remedy, while it looks attractive, relies on the Engineer actually requesting such evidence – he may not be inclined to do so.

## **GCC FORM OF CONTRACT**

The decline in the use of nominated Subcontractors in the construction industry is notable, with a clear example being the absence of such provisions in the GCC 2015 (General Conditions of Contract). The GCC 2015 does not include provisions for nominated Subcontractors due to its requirement for agreement by consent. Forcing a Subcontractor onto the Contractor through nomination would contradict this principle.

Instead, the GCC 2015 introduces the concept of a "selected Subcontractor." In this approach, the Subcontractor is chosen through a process that involves consultation with the Employer, ensuring mutual agreement and consent. The GCC 2015's shift to selected Subcontractors promotes collaboration and accountability by involving both the Contractor and Employer in the selection process. This consensual approach reduces disputes, enhances flexibility and control over Subcontractor performance, and increases transparency, improving trust and communication. Ultimately, it fosters a more harmonious and effective project delivery. It also, on the other hand, shifts the risk of Subcontractor works directly onto the Contractor, with no remedy against the Employer for defaults of the Subcontractor.

#### **PROTECTIONS FOR THE CONTRACTOR IF A NOMINATED SUBCONTRACTOR IS APPOINTED**

The contract entered into between the Employer and the Contractor (let's call it the main contract) will address the remedies available to the Contractor for any defaults of the Nominated Subcontractor (if any). An example of this is as mentioned in the JBCC form of contract paragraph above. If the Main Contract is silent in this regard, the Contractor will have no remedies against the Employer. His remedies will lie in the Subcontract agreement. Another example is the requirement (under the FIDIC) for the Employer to indemnify the Contractor if he appoints the nominated Subcontractor where reasonable objection is raised.

#### **PROTECTIONS FOR THE NOMINATED SUBCONTRACTOR AGAINST DEFAULTS OF THE CONTRACTOR**

We have often been asked by our clients who are appointed as nominated subcontractors – *"The Contractor hasn't paid me; can I go directly to the Employer for payment?"*

In *Minister of Public Works and Land Affairs v Group Five Building Ltd [1999]*, the Court delineated the essential elements of a nominated subcontractor. The first element established is that the Employer reserves the right to nominate specific persons to perform defined parts of the overall works. The second element mandates that the Contractor must accept the nomination, albeit with a limited, yet significant, right of challenge. The third element requires the Contractor to enter into a subcontract with the nominated person, typically under similar terms regarding performance as those in the main contract. **The fourth element clarified that there is no privity of contract between the Employer and the Subcontractor.** The CIDB approved standard form contracts have all been drafted in this fashion.

This lack of privity means – No, you would not be able to approach the Employer directly for payment unless the Employer has agreed to such in a written instrument with all three parties (Employer, Contractor, Subcontractor).

Just as an aside, it is interesting to note that with regards to the fourth element, while the Subcontractor may not approach the Employer directly to secure payment (which, by the way, carries an additional risk should the Contractor become insolvent), there is a benefit to the Subcontractor. Even though the Employer nominates the Subcontractor the Employer cannot sue the Subcontractor for poor work quality, defective work, or delays in completing the project. Instead, the Employer can only enforce its rights under the contract through the Contractor (the fifth element). You will find that standard form contracts may be amended, however, to enable an assignment of the subcontract agreement to the Employer should the Contractor become insolvent – or such main contract is terminated for any reason. This would then mean that the direct relationship with the Employer becomes established through that assignment.

## CONCLUSION

The role of a nominated subcontractor in South Africa's construction industry is defined by a balance of obligations and protections. The Employer's ability to nominate subcontractors ensures specialized tasks are handled by capable entities, while the Contractor retains responsibility for overall project management. Although there is lack of privity between the Employer and the Subcontractor, there have been certain protections built into the standard form contract for

all parties – some of these have been discussed above.

South African law is not well-versed on the topic of Subcontractors shooting the Employer instead of the Contractor, but several key English cases illustrate how this principle can be excepted in practice. In *Junior Books Ltd v Veitchi Co Ltd [1983]*, the House of Lords allowed a nominated Subcontractor to claim against an Employer in tort due to a recognized duty of care, despite no direct contract. This exception, however, is rare and heavily dependent on specific circumstances. In *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd [1994]*, the court emphasized the importance of privity of contract, ruling that only the contracting party could recover losses, even if those losses were suffered by a third party. Conversely, *Darlington Borough Council v Wiltshier Northern Ltd [1995]* demonstrated that an Employer could recover damages for defects even when not a party to the original contract, suggesting some flexibility in third-party claims. Additionally, *Smith and Another v Eric S Bush [1990]*, though not a construction contract case, highlighted that third parties might claim for negligence depending on the foreseeability of reliance and the relationship involved. These cases collectively underscore the nuanced and context-specific nature of a nominated Subcontractors' ability to seek remedies from Employers, emphasizing the importance of clear contractual provisions to navigate these complexities.