Business Case Study: Conflict Management (Panama Canal)

Student Name

Course Number: Course Name

Due Date

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Analysis of the Conflict

Following 3 ½ years of construction, the expansion of the Panama Canal once more became a feature on the global news on the 1st of January 2014. A time when a confederation coordinated by Sacyr, a Spanish construction firm, gave the ACP (Panama Canal Authority), a notice of intent to postpone the building of the Grand Post-Panamax locks because of significant violations that the canal authority was to blame for. This announcement came about due to the body failing to realize a cost increase of $1.625 billion (approximately half of the contract budget).[1] This reawakened arguments over the suitability of giving the contract to GUPC (Grupo Unidos por el Canal).

The consortium sent a letter to the ACP that provided the authority 21 days to pay the budget overruns before interrupting their activities. These extra expenses were blamed on the discrepancies in the information that was handed to the association regarding the implementation of the project and that have been recognized by the Confederate. Moreover, they were attributed to the recurring infringements of the duty to sustain and re-establish the financial balance of the agreement with GUPC because of unexpected events that happened during the construction. The surplus costs were primarily because of the challenges that were faced in the subsoil that were not discovered in the analyses that were formulated by the ACP and the material applied to the creation of marine structural concrete employed in the operations.

The ACP reacted fast to the situation and in a short announcement overruled any form of tension. Furthermore, the authority required that the consortium acknowledges the stipulations of

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[1] Cornell University, "The Panama Canal Expansion Dispute," *Cornell International Law Journal Online*, last modified January 31, 2014, http://cornellilj.org/the-panama-canal-expansion-dispute/.

the authorized contract. The ACP confirmed that, in harmony with the requirements of the agreement, the resolution of their entitlements was contingent on the arbitration of the Dispute Adjudication Board that had a period of 84 days to make a verdict, and consequent concession through an international committee centered in Miami. The ACP responded to the notice to delay activities by declaring a threat that it was set to enforce the bonds created by the GUPC, compounding to $600 million (supported by Zurich American Insurance Company), and to resume construction with a new contractor.[2]

Still, the bond total was apparently inadequate. In relation to the information issued by the factions concerned, a breach of contract would have implied an extra expense of €2 billion and would have postponed the end of the construction till 2018. As a result, it was evident that the dissolution of the contract would not have helped either faction. The pronouncement of deferment of activities led to an 8.95 decline in Sacyr stocks in the first trading session of 2014. A few months before, at the close of 2013, Sacyr was a growth frontrunner on the IBEX 35, with a gain of 119 percent in a year.[3] In the meantime, on the other side of the Atlantic, the termination of work was an essential theme of contention in the Panamanian presidential elections that were conducted on the 4th of May.

After that instance verbal disputes followed, going to the severe extent that the consortium decided to make its notice for work suspension operative. With the exemption of maintenance activities, all construction work was halted on the 7th of February. Just then, GUPC had finished 66% of the expansion plan and was rewarded two-thirds of the initial contract amount. The

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[2] Ibid.

[3] Jason, Margolis, "After Six Years and Billions of Dollars, the Panama Canal Expansion May Grind to a Halt," *Public Radio International*, Last modified January 10, 2014, https://www.pri.org/stories/2014-01-10/after-six-years-and-billions-dollars-panama-canal-expansion-may-grind-halt.

authority had disbursed $2.048 billion of the $3.118 billion of the previous proposal and had transferred $784 million in loans. What is more, the ACP alleged to have given two extra expenses: one for the sum of $156 million to deal with deviations in the cost of steel and the cost of fuel; and an additional $20 million for recruitment needs. At that time, the ACP was only ready to pay an added $283 million, contrasted with more than $1.6 billion needed by the contractor.[4]

Analysis of the Negotiation

In the effort to look for an answer the guarantor, Zurich ineffectively tried to resolve the two positions, proposing to change the $600 million bond to advances to the consortium. This was on the precondition that the authority provisionally stops to request the reimbursement of the loans and pay out the more than $500 million in reimbursements awaiting from the budget.[5] Possessing this proposal allowed Zurich to alter its bond risk to credit risk (the authority would have had to pay out more than the sum unsettled in the budget and GUPC would have had to contract debt while anticipating for the negotiation body identified in the contract to clear up its claims). This came with a devotion to complete the construction in June 2015.

Nevertheless, the key hindrance was in the suspension on settlement of the loans. This was because the Panama Canal Authority had maintained that it be reimbursed on completion of the construction. Ultimately, after 50 days of arbitrations and negotiations between the administrations of Panama, Italy, and Spain, on the 20th of February 2014, the first agreement was made, that allowed the building of the third set of locks to recommence. On the 13th of

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[4] Ibid.

[5] Ramon, Munoz, "Panama Canal Project: Panama Celebrates Newly Expanded Canal as a Patriotic Milestone," *EL PAÍS*, last modified June 27, 2016, http://elpais.com/elpais/2016/06/27/inenglish/1467036970_381545.html.

March, the board of the authority agreed to the signing of the subsequent Memorandum of Understanding, establishing a new time limit for the conclusion of operations in December 2015.[6]

The ACP confirmed that possessing a plan B reinforces the mediation process. In the course of the extension of the canal, work did not go as scheduled all the time. There arose labor disagreements, leaks, and construction deferments. For instance, when disputes with the first development consortium became problematical, the ACP strived to create available substitutes with new contractors and suppliers. The authority acknowledged the shift might have led to cost increases or postponements. Moreover, they were willing to appreciate the construction contracts' disagreement resolution procedures. Provided solid contingency preparation, the ACP had the capability to execute its plan B if it saw the need. When the authority had the answer with the chief contractor, it did not need to employ its plan B. However, the ACP apparently displayed rigorous management.

Conclusion

The Panama Canal expansion disaster permits everyone to reconsider a standard issue in public procurement – the adjustment of contracts – for which there does not appear to be a permanent answer. Additionally, this is a long-term challenge in our modern time, one which has been the spotlight of different organizations as one of the core reasons for corruption and swindling in public procurement (OECD, 2006 and European Commission, 2014). Neglect of this feature does hinder not only fair competition and the standards of transparency, but also bear severe consequences for public accounts due to the amplified inconvenience resulting from the realization of contracts.

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[6] Alex, Wright, "Full Speed Ahead - Risk & Insurance: Risk & Insurance," *Risk & Insurance*, last modified March 25, 2014, http://riskandinsurance.com/full-speed-ahead/.

This scenario requires actual proper and stern execution of the regulations. Still, in the first place, it is also significant to enforce other forms of measures to avert conflicting interests (private and public) from being wrongly biased. These actions are comprised of instituting open and unequivocal regulations (that would both restrict the margin of discretion of the contracting bodies and prohibit carelessly low bidding), observing the alterations of the tenderers, and launching a dispute resolution scheme that assures effectiveness and independence (in finances and time). If these points are put into thought, this analysis borrows some classic experiences from the case under review that can be deduced to any public procurement system.

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