

Contracting - Organization or Annihilation

The Consultant's Viewpoint — by B. D. Ballin (Fellow) and R. Morledge (Associate)

The Building Industry has always been high on the list of bankruptcies; it not only has more bankruptcies than virtually any other industry but its percentage of registered firms going bankrupt is alarming.

This high rate of bankruptcy is not just bad luck; we consider it results from mismanagement and inefficiency. We do not pretend that the answer is easy but in this article we hope to highlight some of the pitfalls and to suggest some ways in which the contracting industry could improve its efficiency. There is no simple wonder cure; it is a straight-forward case of organization and discipline — having the correct system and sticking to it.

Our thoughts, though not particularly original will, we hope, point the way. The facts are staring every Contractor in the face each time he enters into a contract.

Compliance with the Contract

Despite the fact that his profits or his very existence relies upon complying with the terms of the contract, for some reason this is disregarded and the path to the bankruptcy court is chosen instead.

We have seen companies that have been built up from nothing in a matter of a few years, to turn over in excess of a million pounds; built up through sheer hard work and determination of those who first conceived the idea; built up with enthusiasm such that they deserved to succeed; BUT THEY FAILED because they did not insist that those who were subsequently employed were effective to enable the company to grow stronger and consolidate.

It is not good enough merely to employ good Estimators and good Contract Managers; production of the documentation that is required to comply with contracts under which the company is operating is essential.

SOME FAILURES

The following are a few of the more likely methods of losing money. These are not necessarily listed in the order of importance or in the order of their "popularity".

Estimating

To win a contract by "blind" estimating, i.e. based on theoretical or assumed costs, is almost certain to be disastrous. Effective feed-back is essential. (This is referred to later)

Contract Documents

These can be considered under two basic headings (a) the main contract document (b) the sub-contract document. Firstly one might consider that the prime fault in connection with contract documents is that some contractors actually execute projects without them. Hardly any wonder that there is misunderstanding regarding the extent of the work envisaged by each party. They then often end up executing work for which they receive no payment whatsoever. This is an excellent method for losing money.

Secondly, and just as foolhardy, is to have conditions in the sub-contractor's document less rigorous to the main contractor than his own conditions with the building owner. In these circumstances it is quite usual to find that the main contractor is duly required to pay the sub-contractor for an item which he is unable to recover from

the building owner. The slippery slide again.

Instructions

To secure a loss on the contract:— execute work without written instruction or without any instruction — how often do we hear from well meaning site personnel "Well it was obviously required, wasn't it?", "The Clerk of Works asked for it" or, "The architect said we ought to do it". Was it obvious? Was it instructed? Was it confirmed? Was it recorded?

"NO INSTRUCTIONS = NO PAYMENT = LOSS"
Obvious, but a fault repeated endlessly.

SOME SUGGESTIONS

Site Feed-Back for Estimating Purposes

In many cases there is a lack of effective site feed-back. The ideal of an accurate breakdown of on-site resources to recognisable operations is very often not achieved because (a) the requirement of the site staff is over-tedious, time consuming, or is not properly controlled, or (b) the estimator does not make proper use of the supplied information.

An estimator who does not refer to contemporaneous records is effectively "guessing", although the guess may be educated or within reasonable bounds — "blind estimating". This means that the estimated future cost of the contract is not directly based on the company's current output and often results in optimistic estimating brought about by the pressure of tight and highly competitive tendering.

The obvious result of such a breakdown is that successful tenders are potentially loss-making before commencement on site.

Method Statements and Discussions for Estimating Purposes

An area where contractor's management seems to break down is in the liaison between estimating and contract management. It is of course critical that methods to be used in future projects are discussed, particularly where the use of expensive plant is being considered. Such methods where the estimator bases his estimated future costs upon them are best recorded, to be referred back to if the tender is successful. The often found lack of this sort of method statement tends to lead to contract management building to their own methods without considering values budgeted, or originally considered methods, with the inevitable effect on profit margins.

Cost Control and Cost/Value Comparison

Good management principles demand that financial progress of business is monitored regularly to enable action to be taken where problems begin to occur.

One of the singular breakdowns in contract management is the lack of such an effective system in many small or medium sized firms. They may well have a system that purports to compare cost with value — (Value = Estimated Cost + Overheads and Profit) but this is often so historical as to effectively indicate only which hole the money went down!

Sometimes as much as 4-6 weeks may pass before this information is available in a form to be of any use to management. By this time of course, the construction

industry's characteristic short term operations, and more particularly, the loss making one, has ended.

To some extent in these cases, management is working in the dark with out-of-date information and is therefore ineffective in control.

It is of course quite possible and with a *minimum* of additional overhead cost, to incorporate an integrated budgeting scheme into the company management where such a scheme will indicate almost immediately any site cost problems and therefore allow fast remedial action.

Contractual Administration

Probably the commonest area where real problems occur is in the administration of the contract in legal terms.

Many firms are still unaware of their simplest rights and obligations under (even) standard forms of contract!

Conditions precedent, such as the need for instructions to be in writing, giving notices to sub-contractors, etc., are often ignored with dire financial consequences.

Proper notice of negative and positive claims at the time of the occurrence and not weeks or months after, is often not given, which is hardly conducive to a sympathetic consideration of any claim.

Passing on contract obligations to sub-contractors is often attempted by exchange of letters, conditions on the backs of orders, or ineffectual statements such as "in accordance with the conditions of the main contract" which fail when a dispute gets to court. Standard sub-contract forms are readily available and simple to use.

Lack of Management Training

It is an unfortunate truth that the construction industry is slow to train for promotion. Promotion is (rightly) gained upon merit, but a man promoted from Foreman to Site Manager or Site Manager to Contracts Manager is rarely given the appropriate training for his new level of responsibility. As a result an administrative or contractual or managerial error occurs which is often irreversible and is financially injurious; of course the man is blamed and possibly even used as the proverbial "scape goat" but the pattern (only too common) is due to bad basic policy.

Over-trading

The fluctuating demand in the industry gives business temptations to contractors in times of boom that are difficult to ignore. Attempts at fast expansion to meet the new wealth of business are often disastrous, resulting in cash crisis and often insolvency; and at times, such as now, when businesses have to contract to meet the low level of work, they find it impossible.

This must reflect the low capital investment in plant and buildings in the industry and the ease of availability of short term high interest finance through the banks. These reasons, together with the tendency for material suppliers to extend credit in an almost "kamikaze" fashion, complete the formula for disaster.

A level headed board of directors with one eye on their borrowing "gearing" will live through the slump to fight another day, sometimes because they have already learnt that all that glitters is not good company policy.

On the more day-to-day basis a company whose finances are too highly geared will find that a loss-making contract, or a single dispute involving a medium amount

of cost which is held up awaiting arbitration, can bring them to their knees.

ON SITE

Delays can be Expensive

A contractor can be delayed on site for numerous reasons most, if not all, of which would be covered by the contract between themselves and the employer, which, in the case of the RIBA Form of Contract, is Clause 23. It would, however, appear that the contractor is only entitled to an extension of time if delayed by reason of one of the named clauses, but this view is not shared by all the experts.

Delays can occur even before the contractor enters upon site, perhaps because the site is withheld from him beyond the date stated in the contract or because he is awaiting information to enable him to commence work, e.g. setting out details.

Most common are delays which occur during the course of the works and, not wishing here to recite those listed in the contract, the two which probably spring to the mind most readily are delays which occur due to the fact that information is awaited from the Architect (or other source) or delays occurring due to exceptionally inclement weather. The latter point is probably worth a thought; that the contract clearly states that the contractor is only entitled to a delay if the inclement weather is "exceptional", he is not entitled to a delay merely because he encounters inclement weather. We would submit that a contractor *would not* be entitled to a delay if he lost five to ten days work due to rain, frost etc. during January, as he would have been expected to plan for at least this much lost time during the winter month. He *would* however, we would submit, be entitled to an extension of time if he lost five to ten days due to continuous rain during June (as he obviously would not expect to lose time during the reputedly hot season). *Exceptionally* inclement weather could be defined by weather which exceeds the average for any one particular month by a degree.

Therefore each circumstance must be expertly considered based upon *recorded* events considered in relation to the terms of the applicable contract.

Delays – Their Notification

Should such circumstances occur that are covered by the relevant clause in a particular contract under which a contractor is acting, then he is *entitled* to an extension of time, but it is a condition precedent to that extension being granted that certain procedures are followed, e.g. he shall notify the architect in *writing* as soon as that delay becomes evident and it is then up to the architect, not the contractor, to assess the extent of the delay which the contractor has suffered. The assessment by the architect may be considered strange as the contractor is in a better position to assess the extent of his delay from his planned programme, but in order to seek the protection of the contract, one must act in accordance with it and merely advise the architect that the delay has occurred. The architect in his infinite wisdom may in fact ask the contractor to furnish details of the delay he considers he has suffered, which then entitles the contractor to present a case. The situation is also similar for any costs which are related to a delay, where such costs are payable under the contract.

Delays and the Architect

The important point to note here is that all the contractor must do is notify the architect, but that notification must be in writing. Having done that the contractor has discharged his obligation and the architect cannot contend at the end of the contract that the contractor failed to furnish details or state the extent of his delay, because this is the architect's responsibility.

We feel quite certain that a number of contractors do not send these formal letters to architects for fear of upsetting an officer to the contract who is in a position to make life difficult for them or to prejudice their chances of getting work from the architect. We would suggest that these fears are unfounded; the architect will be satisfied provided the contractor complies with the requirements of the contract which the architect's employer, the building owner, has selected to use for the particular project.

Recording Delays and Information

One very easy way of recording two of the items listed as items giving the contractor entitlement to an extension of time is for these to be recorded at every regular site meeting.

The particular causes for extension of time to which we refer are those of "awaiting information" and the "exceptionally inclement weather". It is suggested that an item should be put into the site minutes of every site meeting under the headings of "Delays Incurred by Inclement Weather" and "Information Awaited from Architect" and, to be fair, it might be advisable also to have a third heading which could be entitled "Information awaited from Contractor". It is suggested that the headings should be incorporated into the minutes regardless of whether the entry under these headings would be "NIL", the reason being that at a later time in the contract to look back and see such entries is informative in itself - every picture tells a story.

Site Minutes

It will therefore be noted that we consider that these have a very important function to perform in the contract. It is not just sufficient for the architect to visit the site regularly each week or when requested by the contractor to sort out a problem, and leave the site. We contend that formal site meetings, with minutes confirming the events since the previous site meeting, play a valuable role in ascertaining at the end of the contract the events that have occurred during that contract, e.g. whether the contractor was on programme or when he was delayed and the cause of those delays, or whether he was held up for information and when those events occurred. It is also possible to detect whether he could have been executing other work or whether he was at a standstill if he was awaiting information.

We would therefore suggest as an item of efficiency, that regular formal site meetings with minutes taken to a standard format are vitally important in the smooth running of the contract and create an amicable atmosphere between the parties involved in that contract rather than the contrary.

The meetings *should be small* (and therefore effective), just the architect and contractor's representatives, possibly the quantity surveyor (when the subject matter is relevant) and also relevant sub-contractors' representatives, only present however for the duration that their work is discussed.

Site Instructions

Whether receiving instructions from the architect or giving instructions to the sub-contractor, the contract is quite conclusive that those instructions given verbally, shall be confirmed in writing as the condition precedent to payment. Unfortunately many contractors fail to do this; again perhaps from an attitude of not wishing to antagonise the architect in continual confirmation; most architects, we are sure, welcome a contractor who complies with the contract as this avoids disputes at a later date and also avoids any animosity which could occur if there is a dispute regarding the precise nature of the verbal instruction that was not confirmed.

THE COST

Final Recovery

The ability of the contractor's surveying staff to maximise the recovery of costs is only as good as the documentation generated by the site staff. No matter how highly qualified a surveyor may be he cannot write with his hands tied behind his back!

It is, however, in the surveyor's interest to ensure sufficient liaison with the contracts managers to avoid that problem occurring. Upper management should ensure, by company policy, that this liaison exists at *all* levels, and this we cannot stress too strongly.

Our Final Conclusions as Consultants

Professional quantity surveyors during the normal course of their duty, particularly in the post-contract field, are continually made aware of the shortcomings of the contractor's organisation, with particular reference to the documentation. Equally, by the very nature of their profession, the Contractor's surveyors with their intimate knowledge of the contract and their practical knowledge of building construction, are ideally suited to assist the contracts manager to ensure that the project is not only built, and on time, but that he is able to recover the contractor's full financial entitlement. Unfortunately contracts managers often seem reluctant to ask for such assistance, or the contractor's policy does not encourage such liaison. In either event the result is the same - reduced efficiency and lower financial recovery.

THE ROLE OF THE QUANTITY SURVEYOR is changing and we consider, and have found from our experience, that the more experienced and senior surveyor is ideally suited, from his broad knowledge and almost inevitable contact with all departments, to investigate and comment upon the efficiency of his contracting organisation. Unfortunately his comments are often restrained and his voice muffled when the areas of inefficiency are revealed, as often this requires criticism of the parties which sign his monthly pay cheque! Most forward thinking and outward looking companies welcome constructive criticism, although having considered it they may, for other external considerations, reject it. Any constructive suggestions that can be made, should be made, as any company can only be as good as the staff it employs.

The Country needs an efficient building industry; the building industry must be efficient to survive. In the present small market, efficiency is an essential ingredient to survival. Streamlining and development of a system, which must be the *right* system, will provide the solid foundation on which the future expansion, which will surely come, can be built.