Giving the contractor free rein?

Elizabeth Jones asks whether the JCT Management Contract is a contractors charter

The construction industry has now spent some 18 months attempting to convince clients and potential clients that management contracting, usually under the *JCT 87* form or a bastardised version of this document, or that even more exotic alternative – construction management – offer new and improved methods of getting what a client wants done – a building built to time, to budget and to standard.

The advantages proffered range from "having the contractor on the employer's side" – quite what a court would make of this when they are suing each other is somewhat difficult to imagine – and "it means the contractors can start to mobilise and plan earlier" – probably true.

A recent conference at Reading University showed clearly that informed clients remain confused and sceptical – and this is before the new standard form of management contract has hit the courts. Comments ranged from "there has to be a . . . question mark as to whether . . . management contracting will actually bring any benefit to some clients" (Barclays Bank) to "as a client I have to say there is no point in me paying management contractors . . . if I am going to do the job for them myself" (PSA).

Whatever the philosophical advantages of having the contractor as part of the professional team on the employer's side in terms of getting the work done with less friction, in legal terms the document is a contractor's charter in that it offers a virtual cost-plus payments mechanism to the management contractor. Liability is effectively limited to his professional negligence in managing the works – a liability as yet untested in the courts. There is effectively no liability on the management contractor for quality of workmanship or completion to time as both of these are caught by the back-to-back provisions of the document. These provide that the management contractor will exercise whatever rights he has against the works contractor and pass back what he can collect to the employer but no more. He is in the happy position of being able to require indemnification by the employer if he, the management contractor, cannot recover all his losses from the works contractor.

There is also a legal question mark over the operation of the mechanism, in that the managing contractor is trying to collect losses suffered not by himself but by the employer. The works contract rather naively attempts to deal with this conundrum by providing that the works contractor in defending a claim for damages from a management contractor will not plead (as is true) that no loss has been suffered. Quite what a court will make of this is a matter for enjoyable speculation, but will not assist an employer who has suffered loss and must otherwise rely on the *Employer-Works Contractor Agreement*, an adequate but uninspiring document which has unfortunately failed to take account of the sophistication of the current commercial property market where funders, purchasers and tenants all require warranties as to workmanship. Who has the workmanship liability under the *JCT Management Contract?* – the works contractor. Regrettably no provision for the giving of warranties to tenants or for novation to funders appears in either the *Employer-Works Contractor Agreement* or the works contract itself and although both can be assigned, the various parties requiring warranties are not likely to be content with a multi-party assignment.

The management contractor therefore effectively suffers no penalty or loss as a result of failure to complete the building to the prescribed quality and within the prescribed time. As far as cost control is concerned, under the basic form of management contract the management contractor has a fixed fee but otherwise collects his costs for on-sites and materials and is effectively paid on a cost-plus basis for the carrying out of the construction work which is subcontracted under the works contract form on a traditional lump sum remeasure basis.

It is possible to turn the off-sites and materials into a fixed price and this cannot but be recommended as an end to cost control. Obviously it is extremely important that the list of items to be included in the lump sum provision is exhaustive. Otherwise there is a cost plan which is established at the outset and which is supposed to set the parameters of the cost of the work. In reality there is little or no incentive for the management contractor to control costs, as his fee is unaltered regardless of whether or not the job comes in on or under target or not. If the fee is expressed as a percentage it could be argued that there is no incentive at all.

It is arguable that there should be a bonus penalty mechanism on the fee to take account of the contractor's success or otherwise in controlling costs, or even the American device of a guaranteed maximum price, whereby any overrun of cost beyond the originally agreed price comes out of the contractor's fee. This device, often known as an upset price for obvious reasons, is known to most contractors who have worked overseas, particularly in the Middle East, and it should not be beyond the capacity of UK organisations to cope with such provisions in the much more favourable conditions of UK contracting. The management contractor is obliged to secure the carrying out of the works. He is as a means to this (and as a means of qualifying that obligation?) directed *inter alia* to let the works contracts and cooperate with the professional team. What does this mean? Does he not cooperate with these people anyway? What are the contractor's liabilities to manage them in terms of compliance with the programme? If he does not manage them in this way who does? What is the liability of the management contractor if the professionals fail to comply with the programme and there are delays?

These are just some of the questions raised by the rather vague (in legal terms) working of the document which will not be answered until one or more cases have been brought to court.

With regard to the back-to-back structure of the contracts, the device of liquidated damages is retained.

The problem is that LADS do not usually remotely cover the real cost to an employer, particularly a developer, of failure to complete on time. In order for a contractor – in this case the works contractors – to price the works, certainty is however traditionally needed. Most contractors will run a mile if presented with a liability for damages at large. In fact, the so-called remoteness rules which operate to limit the recovery of consequential losses will not extend their liability to prohibitive levels.

Two possible solutions present themselves. One is insurance against consequential loss, the other is limitation of liability to the loss of rent suffered or extra interest payments made as a direct result of the delay. The form of management contract together with

the works contracts do nothing to address this dilemma.

All in all the JCT 87 Management Form of contract bears all the hallmarks of the horse designed by committee. Produced with much painful effort to meet the desire of the UK contracting industry for a catch-all standard form which would replace the one off management contract previously produced by developers and others, it appears to fall between all stools; as a record of the legal obligations of the parties it is defective – the back-to-back damages provisions mentioned earlier are matched by confusion as to the status of the parties prior to signature of the second part of the document; as a means of controlling the time, cost and quality of a project to a client it fails to give the necessary incentives; it also does the contractor a disservice by building in the old chestnut of an architect/contract administrator, who will carry out his traditional arms-length role of certifier and valuer when in reality the contractor would, by all accounts rather have full control of the project, design function and all and the client needs to employ one of those new breed of consultants who can avoid him having, in the words of the PSA 'to do the management contractor's job for them" – a project manager.

Perhaps the trend in the industry towards precisely this kind of structure using design and build forms of contract will solve the problem, spurred on by a recession which appears more and more likely.

The *JCT87* form may then be left behind as a relic of an era, its inconsistencies to be fought over in the courts to the disadvantage most probably of those employers (or their professional advisers) who embraced it too enthusiastically and used it without modification.

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Should our offer be of interest. .

The future credibility of the Code of Procedure for Single Stage Selective Tendering lies with the QS says to Jonathan King

The *Code of Procedure for Single Stage Selective Tendering* is rightly widely respected as a document. The document is prepared by the National Joint Consultative Committee for Building and therefore synthesises the views of all the major participants in the building industry. Contractors, architects and quantity surveyors generally accept the code and it is usual for tender invitations to prescribe that the tender procedure will be in accordance with it.

The public perception of the construction industry, based perhaps on unfortunate experiences with domestic building works and headlines when major projects are in delay, is often one of an old fashioned and inefficient industry where business is conducted in an adversarial manner, usually at the client's expense. Documents such as the Code of Procedure help to present to the industry's clients an alternative impression of competence and professionalism.

It is therefore disappointing to gain, increasingly, an impression that adherence to the code is not regarded universally as essential.

"Should our offer be of interest there are a number of matters which we would wish to discuss before entering into contract." These words, or variations on the theme, are increasingly seen on covering letters enclosing the contractor's form of tender. The wording is clever in that it seeks to introduce a negotiating stage into the tender process and it is not obvious that the letter constitutes a qualification to the tender.

The code defines a "qualification" as a matter which (in the opinion of the architect) conveys an unfair advantage on the tenderer. It is not immediately apparent whether or not the "number of matters" which the contractor wishes to discuss convey such an advantage or whether they are merely matters of clarification.

However the letter is definitely not in accordance with the code which envisages that a tender shall be unconditional and shall comprise a formal offer which the employer is open to accept and thereby establish a binding contract.

It is my impression that contractors are very conscious of the requirement of the code not to divulge their tender price prior to the date and time for the submission of tenders. (There are obvious good commercial as well as professional reasons for this.) However agencies exist which will receive and record details of tenders submitted by contractors and will pass these to all the tenderers after the date and time set. Therefore when the quantity surveyor telephones the lowest tender to call for his priced bills of quantities, if these have not been submitted already he may find that the tenderer is already aware not only that his tender is lowest but also the amount of the difference to the second lowest tender.

If the quantity surveyor falls into the trap set by the letter and allows a negotiation stage to develop he will therefore be negotiating with a tenderer who probably knows the upper limit to which he will seek, by negotiation, to enhance his tender.

The correct procedure, as envisaged in the code, is of course simply to require the contractor to withdraw his covering letter and, if he refuses to do so, to disqualify the tender and proceed to examination of the next tender. In practice the tenderer, if presented with a resolute and uncompromising requirement to withdraw the qualification, will usually stand by his tender. The marginal benefit he might achieve by a modest negotiated increase is greatly out-weighed by the risk of his tender being disqualified and his losing the business altogether.

If the quantity surveyor takes the alternative pragmatic view that it is better to ask his client to pay a little more than the lowest tender than the full extra cost of going to the second lowest then he is failing to meet his obligations under the code and is actually encouraging contractors to submit qualified tenders in future.

The future credibility of the code is in the hands of quantity surveyors. Those in contracting organisations can discourage and discontinue the practice of submitting covering letters and can avail themselves more of the facility to clarify any perceived ambiguity or omission in the tender documents before the date for return of tenders.

Those quantity surveyors in private practice directly appointed by the employer must take a firm position regarding qualifications and ensure that their other obligations under the code, particularly those relating to the prompt notification of unsuccessful tenderers, are rigorously observed.

We are all aware of the practices in property transactions, eg "gazumping", which have led to calls for a Code of Procedure. It would be regrettable if our practices in tendering building works fell into similar disrepute.

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