

# CONFERENCE ON "AVOIDING & RESOLVING DISPUTES IN CONSTRUCTION CONTRACTS"

CLAIMS OF THE CONTRACTOR AND CLAIMS OF THE EMPLOYER  
DELIVERED AT A CONFERENCE ORGANIZED BY THE ASIA BUSINESS FORUM  
ON 6-11-08

## 1. **INTRODUCTION**

### 1.1 **General**

In order to understand the rights of the respective parties to construction contracts, i.e. the employer and the contractor, it is necessary to first the opposing parties' obligations as the converse will represent the other party's rights and hence claims.

It needs to be noted that so-called "construction law" is a corpus of case law which represents the set of rules of law which are applicable to construction contracts and which assist in the interpretation of the latter. It should however be noted that the case law is often reflected in the standard forms of engineering and construction contracts.

As such, this paper will seek to outline the relevant rules of law applicable to the current topic and then examine how three standard forms of contracts in common use in Malaysia accommodate or attempt to circumvent them. These forms of contracts are PWD 203 (Rev. 10/83), PAM 1998, and FIDIC 1999 ("the Silverbook").

### 1.2 **In Brief**

Very briefly, a contractor undertakes in return for a 1) pre-agreed sum of money to be paid by an employer 2) to build and 3) complete the relevant works as defined in the drawings and specifications prepared by the employer 4) at a site provided 5) within an agreed duration.

It can be seen from the above that 1) and 4) are elements the obligations of an employer whereas 2), 3) and 5) are the obligations of a contractor. From this very brief description of what a construction contract is about, the rights (and hence claims) of the two primary parties to every construction contract can be discerned.

## **OBLIGATIONS OF THE CONTRACTOR AND CLAIMS OF THE EMPLOYER**

### **2.1 Obligation to complete**

*Hudson's* emphasizes that construction contracts represent entire or whole obligations undertaken by contractors to construct and complete the works and supply the materials required by the contract. *Hudson's* talks about the early English cases which set out that a contractor who due to his own reasons, without default by his employer abandons the works before completion will not be able to recover payment for the works done to abandonment. This situation while probably still remaining good law is archaic in that almost all modern day construction contracts allow for interim payments to be made, with evaluations to be based on the progress achieved by the contractor.

The point which remains relevant is that a construction contract is one continuous undertaking by the contractor to execute and complete the works, as against certain forms of contracts wherein the various stages are considered to be installments which are severable from each other. In other words, when a building contractor undertakes to carry out works for a contractor, what he in effect agrees to do is to complete the entire works in return for the entire contract sum. Thus not only has the contractor to complete the works, the contractor must also be allowed to complete. If the contractor fails to do so due either to his own default or due to the employer's default then the normal rules in respect of damages apply, on top of anything specifically spelt out in the contract.

#### **2.1.1 What is within the scope of a construction contract?**

This section will be confined to an employer's rights in the event of the contractor's default. The converse will be dealt with in another section below.

The first issue which needs to be dealt with is to ascertain what exactly a contractor undertakes to do. Most contracts will include the requirement that the contractor is to provide everything that is necessary to complete the whole of the works. In this respect, it is interesting to contrast the following two cases:

Case 1 – about 1,000 m<sup>3</sup> of rocks at a site of about 100,000 m<sup>2</sup> in area

Salient facts:

1. About 40,000m<sup>3</sup> of structural excavation allowed for in Bills of Quantities
2. 10 boreholes were carried out by the employer as a part of the pre-award soil investigation which did not indicate any rocks within the designed depths of excavation
3. There is no sum allowed for prime cost ("PC") items
4. The contract allowed for the following:
  - a. Method of measurement - the rates for items of works deemed to include all other works necessary to carry out and complete the particular items
  - b. The contractor is entitled under the contract conditions to claim for costs arising out of "unforeseeable physical conditions"

The question is whether the contractor is entitled to claim for the rock excavation. If the excavation of rock is included as a part of the contract scope, then the contractor cannot claim. It is apparent that the contractor cannot claim to vary the rate for suitable excavation due to the effective and all encompassing "deemed to be included" clause.

Then, the contractor's recourse is to claim for the rock excavation on the basis that it constituted an "unforeseeable physical condition".

So, the question then is "is it an unforeseeable physical condition"? It would seem that due to the actual quantity of rocks, i.e. only 1,000 m<sup>3</sup> spread over 100,000 m<sup>2</sup> and compared to a total of 40,000 m<sup>3</sup>, and with a total of about 10 boreholes (with each borehole corresponding to about 10,000 m<sup>2</sup> of area) provided, it is reasonable that presence of rocks may be missed and therefore, it is arguable that the presence of about 1,000 m<sup>3</sup> of rocks is not unforeseeable. The case will probably be different if the quantity of rocks is say about 10,000 m<sup>3</sup>.

Case 2 – structural steel support to ceiling above a hall as part of the construction of a major building complex

Salient facts (these have been distorted to hide the identity of an ongoing project):

1. Contract sum is RM 400 million
2. The contract is on a lump sum basis with amounts indicated against items of works in the summary of tender which forms a part of the contract
3. About RM 30 million allowed for PC and provisional sums, including some RM 3 million for "Contingency"
4. There was an item described as "structural steel trusses to support **roofs** at" all relevant buildings - (emphasis added)
5. An item of the Works (not connected with the works in issue) under nominated sub-contractor's ("NSC") scope indicated that it shall be constructed to "Specialist's Details"

6. The steel truss support in respect of ceiling (not disputed as being under main contractor's scope) above a hall also indicated that it was to be constructed to "Specialist's Details"
7. The item in the summary of tender for the ceiling did not mention the support structure

The question is "is the contractor obliged to provide the support system to the ceiling without entitlement to claim"?

The following factors seem to militate against the support structure being within the contractor's scope:

1. The fact of a substantial allowance for works to be carried out by NSCs
2. The use of the description "Specialist's Details" for other works by an NSC
3. Even if there is an effective "deemed to be included" clause, the allowance of substantial "Prime Cost" and Provisional sums open a loophole

In the current case the contractor can argue very effectively that he had acted reasonably when tendering for the contract works that he did not allow for the support structure as he had assumed that it will be carried out by an NSC to be appointed by the employer. This contrasts with Case 1 where the contractor is to be the only party who will be carrying out works.

It therefore follows from the above two cases that the documents comprising a contract have to be examined carefully to determine what is within the scope of the contractor's undertaking and what is not. The lesson for the drafters of contracts is that all the documents especially the breakdown of the contract price and the drawings will need to be carefully scrutinized and the annotation of drawings cannot be left

entirely to draftsmen. It is essential that the latter may need to be checked by even the contracts personnel.

### The position at law

At law the temporary works is entirely within the prerogative of the contractor. This will be the case even if the temporary works are specified by the employer (normally his architect or engineer). The facts of two cases illustrate this very strict rule:

1. The specifications for the sinking of foundations within the River Thames required the sinking of caissons and provided the details of the caisson. The caisson was subsequently found to have been inadequate and collapsed under the pressure of the water. The contractor sued for the extra costs incurred. Held – the contractor takes the risk in respect of the adequacy of the specification for temporary works: *Thorn v London County Council* (1876) 1 App. Cas. 120
2. The specified structural steel sections were found to have been too thin for the fabrication of a steel structure. The engineer allowed the contractor to use bigger sections but refused to give the instruction. The judge noted that in inviting the submission of tenders based on the specification, the employer can be said to have effectively asked the contractor “See if you can do this, and tell us what price you can do it for; satisfy yourselves ... whether you can do it before you enter into the contract” : *Tharsis Sulphur & Copper Co. v McElroy & Sons* (1878) 3 App. Cas. 1040.

In other words, the contract undertakes to figuratively “bring the employer to his destination and will be entirely responsible to ensure that it happens”. *Hudson’s* has summed up the position taken in the *Tharsis Sulphur* case very succinctly, i.e. “Can you build to this design, and if so

at what price?"<sup>1</sup>. It appears that the obligation to complete extends to varied works of a similar nature to the main works<sup>2</sup>. By tendering and subsequently accepting an award the contractor is deemed to have agreed that he can do it for the tendered price.

How about a case in which a source of borrow fill has been provided by an employer and at the same time the specification requires that the borrow fill be compacted to a minimum dry density of 1.8T/m<sup>3</sup> which is impossible to achieve with a dry density of only 1.65T/m<sup>3</sup> being achievable, then will a contractor who contracts to compact the material be liable to the employer? In this case there is a fundamental difference from the situation in *Tharsis Sulphur* in that the physical properties of steel is common knowledge whereas only the employer's consultants had the means of ascertaining the maximum dry density of the fill material.

*Provisions in the standard forms of construction contracts in respect of temporary works* – both PAM 1998 and PWD 203 only contain provisions that the contractor shall be fully responsible to comply with the required standards, any approvals given or failure to detect non-compliance at an earlier date notwithstanding (PAM at clause 6 and PWD at clause 9(b)). The only provision which touch on temporary works are those which render the contractor liable for setting out (PAM at clause 5.0 and PWD at clause 14). However, FIDIC which is generally acknowledged to be more complete in terms of the extent of control afforded to the Engineer over the execution of the works by the contractor, very specifically states at clause 3.1(c) that any "approval, check, certificate, consent, examination, inspection, instruction, notice, proposal, request, test, or

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<sup>1</sup> Hudson's 11<sup>th</sup> Edition at paragraph 4.054

<sup>2</sup> Please see the New Zealand case of *Slower v Loddey* (1900) 20 NZLR 321

similar act by the Engineer... .. shall not relieve the Contractor from any responsibility...". This provision obviously includes approval of temporary works.

However, having said this about both PWD and PAM forms, there is nothing to stop the conferment on the S.O./Architect a power to approve temporary works details/design in the specifications and often in the case of PAM Form contracts in the Preliminaries Bill. A lot of contracts do in fact require very extensive obligations on the contractor to submit shop drawings of temporary works (and permanent as well) and the contractor is in such instances deemed to have allowed the required approval times into their programmes.

In cases where there are provisions for temporary works to be approved, this does not give the S.O./Architect/Engineer an open cheque to 1) require revision after revision of submissions of method statements and 2) submission of method statements for each and every temporary works. In the case of 1), the requirement to submit further revisions should be subjected to the requirements of the contract and what is accepted practice. In the case of 2) submissions may be demanded only when required by the contract.

Features of construction contracts which reflect this "entire contract" obligation

*Contractor liable for losses and damage to the works before completion* – whilst in the majority of cases the losses and damage which occur before completion are covered by insurance, contractors have to bear the deductibles and in the event of failure to insure, the contractor bears the risk of damage. This is in respect of losses and damage which occur without any default by the contractor such as for example as a result of fire, flooding or any acts of God. This follows from the fact that the

contractor is responsible to clear all hurdles until the destination is reached.

*Contractor to bear cost of completing the works after termination due to default* – thus if a contractor's employment is terminated due to breach, the additional cost (being the difference between the cost in engaging a 3<sup>rd</sup> party to complete and the cost to complete based on the contract). This follows from the application of the 1<sup>st</sup> limb in *Hadley v Baxendale*, the contractor's undertaking being to complete the whole works.

*Unforeseen ground conditions* – according to *Hudson's*, this is the reason why provisions are included in construction contracts to enable contractors to claim for "unforeseeable physical conditions" (used in FIDIC) as otherwise the fear is that the consequence of the eventuation of such a risk may "break the contractor's back" and consequently adversely impact on the employer's interests. Only FIDIC contains such a provision (at clause 4.12) whereas both PAM and PWD are silent on it. It is interesting to note in this connection that where soil investigation data are provided and adverse ground condition not discernable from the data is encountered, contractors may succeed in claiming. The rationale behind is that such data are provided to help secure more competitive bidding (by reducing or eliminating uncertainty which invariably push up the tender price) and as such when the conditions are in fact worse than they are represented to be, then the employer must foot the bill for the additional cost. The basis at law for the contractor's entitlement is misrepresentation. If there is no representation, then there is no possibility of misrepresentation.

A popular misconception amongst S.O.s

It is a common misunderstanding especially amongst REs and those of similar genre that if an item is included in the specifications or the method of measurement, then the contractor must provide the relevant item without additional entitlement. What they fail to understand is that the specifications are general documents which define the standard that a contractor must comply with in the event that a particular item of work and/or supply is called for elsewhere in the contract, i.e. the bills of quantities and especially the drawings. Below are what the writer would consider to be classic examples:

*Rubble pitching below a bridge* – the method of measurement included an obligation for the contractor to provide cement mortar. There are two types of rubble pitching, one called “dry” pitching and the other “wet” pitching. In fact the drawings indicated dry pitching. The RE insisted that the contractor had to provide the cement mortar, thus upgrading the “dry” pitching into “wet” pitching!

*Painting to wall* – whilst the drawing of the cement rendered wall was silent as to painting, the specification included a section for painting to the wall. Therefore the RE insisted upon painting to the wall. I wonder why didn't the RE insist upon the contractor carrying out bored piling because the specification included a section for bored piling!?

### **2.1.2 Liability for defects**

Due to the position at law as well in the PAM and PWD Forms (PAM at clause 15.1 and PWD at clause 39(b)), the contractor is entitled to have the works certified to be practically complete, notwithstanding the

presence of minor defects and minor works, to the extent that these do not prevent an owner from occupying and using the works for the purpose which they are intended. This is to abuse a predatory employer from exploiting the right to liquidated damages as a means of “earning profit”.

There are two categories of defects, i.e. patent and latent defects. These have different impacts on a contractor’s liabilities in terms of its obligation during the defects liability period (“DLP”). Thus, whilst a contractor is relieved from liability in respect of any defects which are apparent or should be apparent on the expiry of the DLP once the same are rectified, defects which are not apparent at the date of expiry impose liability on the contractor under the Limitation Act 1953. A contractor’s liabilities in respect of patent and latent defects are dealt with below:

- i. Patent defects – the contractor’s obligation in respect of these is to ensure that all defects which are apparent by the end of the DLP and are notified to him by inclusion in the list of defects delivered to him within 14 days of the expiry of the DLP (clause 45(b) of PWD Form and clause 15.2 of PAM Form). Upon rectification, the contractor is entitled to have his obligation in respect of defective works discharged and in both PWD and PAM Forms, the certificates are called the “Certificate of Making Good Defects” (“CMGD”). It therefore follows that in respect of both Forms that any defects missed out in the list of defects cannot be added unless of course the omitted defects are detected and notified within the relevant 14 days’ period. In the case of FIDIC Form the contractor is required to rectify all defects by the end of the “Defects Notification Period”.
- ii. Latent defects – these are defects which by their nature are hidden soon after completion of the relevant works and which may surface later. In the case of the PWD Form, if any such surface after the

issuance of the CMGD but before the payment for the Final Certificate as the common law right to set off is specifically preserved via clause 50 whereas in the case of PAM Form, this common law right has been specifically overridden by clause 30.3(i)<sup>3</sup> as the right to rectify certificates (conferred by clause 30.1) is not applicable in such a situation. The normal rules in respect of limitation apply in respect of latent defects.

### **2.1.3 Employer's remedies in the event of non-compliance of works or materials**

Whilst 2.1.2 deals with the issue of defects during the DLP, the issue of an employer's control of the contractor during the execution of construction to ensure compliance with the specifications also needs to be dealt with. All major forms of contracts contain provisions which empower the employer or his representative to require the removal of non-compliant works and/or materials and to engage a 3<sup>rd</sup> party to do so if the contractor fails to comply (PAM - clause 2.2 read together with clause 6.4, PWD - clause 5(a)(ii), FIDIC - clause 7.6). In such a situation the employer may set off the cost incurred from payments to the contractor, of course with the employer paying to the contractor based on the applicable price in the contract for the works/material. Invariably the cost of removal and reconstruction is higher than the price under the contract. This provision ensures that an employer is not helpless in the face of a "recalcitrant" contractor.

## **2.2 Obligation to complete on time**

Whilst it is generally important that construction projects are completed on time as construction projects are undertaken by developers for

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<sup>3</sup> See also *Pembinaan Leow Tuck Chui & Sons Sdn Bhd v Dr Leela's Medical Centre Sdn Bhd* [1995] 2 MLJ 57

commercial purposes, i.e. start manufacturing (in the event of factories), to sell to purchasers who will in turn be either using the premises as factories or shops or dwellings, it needs to be noted that time is not of the essence in construction contracts. If time is of the essence in a contract, it means that if party which is obliged to comply with any obligation in respect of timing, and if that party fails to comply with the obligation, the aggrieved party is entitled to rescind the contract in the event of failure to complete by the set completion date and recover for damages. If time is not of the essence, then the aggrieved party may only recover damages.

The rationale for this is the fact that to hold that time of the essence will be grossly unfair to the contractor as 1) the contractor has generally expended a lot a money in getting the works done and the conferment of the right to rescind on the basis of time being of the essence will allow termination for very trivial delays, with a day's delay sufficing and 2) the works would have been constructed on the employer's land, thus conferring a not insignificant gain to the employer.

This does not however mean that an employer faced with serious delay by his contractor is without remedy apart from the recovery of liquidated damages. Far from it, as common law does in fact recognize an employer's right to terminate a construction contract in the event of serious delays, with the right extending to cases where it is apparent even before the contractual date for completion that there is no possibility of completion on time or not too long after due completion.

Apart from the right by the employer to terminate in the event the contractor "without reasonable cause wholly suspends the carrying out of the Works" or "fails to proceed regularly or diligently" (PAM clauses 25.1(i) and 25.1(ii) and PWD clauses 51(a)(i) and 51(a)(ii)), and "abandons the Works or otherwise plainly demonstrates the intention not to be continue performance of his obligations under the Contract" (FIDIC clause 15.2(b)),

none of the three relevant forms contain any provision allowing the employer to terminate the contract in the event of serious delays. This probably follows from the fact that as it is often the case that issues of delays are often complicated and as such extremely difficult to ascertain with reasonable accuracy during the course of construction, the exercise of the right of termination based upon very clear and explicit criteria of delay would inevitably be a very risky endeavour.

In such instances it would be much better to terminate the contractor's employment based on the right to do so conferred at law on an employer to accept the contractor's repudiation by the contractor's failing to proceed with such dispatch as will enable the works to be completed by the time stipulated<sup>4</sup>.

### 2.1.3 Consequences of delays by a contractor

We will examine two categories of delays, i.e. delays by contractors to complete on time, i.e. where the contractor delays beyond the date for completion and where the works is delayed but the contract is terminated before the date for completion ("completion date").

*Delay beyond the contract date for completion* – in this situation, the norm is for the employer to recover liquidated damages, this remedy being de rigueur all standard forms of contracts. This does not however mean that an employer will automatically in all cases in which a contractor is in delay in failing to complete within the definition of the contract be entitled to recover the sum stated in the contract. This follows from the provision of S75 of the *Contracts Act 1950* and the interpretation

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<sup>4</sup> Please see for example *Cork Corpn v Rooney* (1881) 7 LR Ir 191

given to it at law<sup>5</sup> that save in those cases where it is not possible to prove the actual damage suffered, a party seeking to recover liquidated damages must prove his actual loss. Thus for example if a developer can show that most of the units in its development have been sold, then he will be likely to recover liquidated damages but if all that is outstanding is the provision of "as-built" drawings in a purely civil engineering construction, such as water mains laying, it is most unlikely that the contractual rate of say RM 5,000.00/day will be recoverable. There have been instances of contractors providing for the recovery of general damages in instances of delays by their sub-contractors. In such instances, they will be able to recover the liquidated damages which they suffer under their main contracts.

If the right to recover liquidated damages by an employer is lost due to for example an act of prevention which cannot be saved by an extension of time, the employer may still recover general damages but in such situation the rate of liquidated damages set under the contract acts as the ceiling to the amount recoverable. This follows from the wording of S75 of the Contracts Act.

*Delay caused before contractual completion date and contract is terminated* – this concerns the situation wherein a developer either terminates a contract either due to serious delay by his contractor or for some other reason (usually to do with serious non-performance culminating in suspension of work) accompanied by delay, in both instances before the completion date. One point of practicality needs to be noted here. Developers faced with contractors in serious delays will normally look at the liquidity of the contractor and if the outlook is positive

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<sup>5</sup> Please see the case of *Selva Kumar a/l Murugiah v Thiagarajah a/l Retnasamy* [1995] 1 MLJ 817

the developer will normally prefer to straggle along with him as the likelihood of recovery of liquidated damages is strong. However, if the contractor's liquidity is doubtful, the developer is likely to terminate the contractor's employment as the first course of action, and any recovery from the contractor is usually seen as a bonus and as such a 2<sup>nd</sup> line of damage control.

There will three possible headings of damages that will be of interest:

- a) The delay caused before termination – the liquidated damages clause cannot apply in such a situation. As such the employer will have to prove the damages suffered in the usual manner;
- b) The delay caused in the exercise to engage a replacement contractor. This will be recoverable as a likely consequence of the termination. Of course, due to the employer's duty to mitigate, the period needs to be reasonable, although the writer has seen almost immediate engagement of a new contractor. A duration of up to about two months should be reasonable (a matter of judgment based on experience) and anything longer is likely to be unreasonable unless there is something unusual about the works or it is of a highly specialized nature which will bring the facts under the first limb in *Hadley v Baxendale*; and
- c) Acceleration cost. Whilst there is no case law which the writer is aware of, it is submitted that the cost will be likely to be recoverable due to the following reasons:
  - i. The cost of moderate acceleration is not much higher than that in prolongation, provided that agreement in its regard is reached before award;

- ii. It is likely to be the case that (again) moderate acceleration of say up to two months as against a year's work will be lower than the cost of the usual liquidated damages and i and ii added together will almost definitely be cheaper.

As such, the cost of moderate acceleration is, it is submitted recoverable as it will be likely to be lower than the cost of delay.

### **3 THE EMPLOYER'S OBLIGATIONS AND CLAIMS OF THE CONTRACTOR**

An employer's obligations can be summarized as follows:

1. To pay the contractor for works (including variations) done
2. To allow the contractor to carry out his works without hindrance

It can generally be said that an employer who commits serious breaches of the first of the above is liable to termination of the contract and claims by the contractor. Breaches in respect of the second normally result in the contractor being entitled to extension of time and occasionally the time for completion being set at large. These shall be examined in detail below.

#### **3.1 Employer's Obligation to Pay**

Lord Denning did in an oft quoted judgment state that "payments are the very lifeblood of the contractor". Unfortunately, contractors can without understanding the overall context of the payment obligation take slight breaches as pretexts for termination of their contracts especially when they have under priced. Having said that, it is almost invariably the contractor who has to suffer in silence when faced with an errant employer. At law, there is no automatic right to consider that an employer has repudiated a contract simply because of delay in discharging its payment obligation, and rightly so. If the law confers such a right, it may enable a contractor who has underpriced a contract to rescind on the occurrence of a single default which may be the result of a simple hiccup by his employer. Rather the law requires that what has to be discerned from the delays in payments is that "the non-delivery or the non-payment amounts to an abandonment of the contract or a refusal to perform it on

the part of the party making the default”<sup>6</sup>. *Hudson’s*<sup>7</sup> has summarized the situation quite elegantly and is as such worth noting:

“So a clear indication or refusal or inability to pay future instalments will be a repudiation, as also a repeated failure to pay on time in response to warnings, if raising the inference of an intention to pay late habitually so as to derive financial advantage, it is submitted. Generally, delay in making payments if sufficiently serious and persisted in after warnings, may, after a suitable notice, justify rescission ...”

It is therefore submitted that a delay by say a month, followed by a warning giving a reasonable grace period to effect payment may justify rescission by giving a notice after the expiry of the grace period. Alternatively, it is again submitted, repeated delinquency of say two weeks in three consecutive payments with a warning against future repetitions may justify termination if the delay is repeated in respect of yet another payment. Withholding of payment certification whilst not mentioned in the case law would it is submitted have the same effect as delays in payments for certified payments. It is quite common for main contractors to blatantly delay certification of works although it is very unusual for architects and engineers to do so.

In the event of rescission, the contractor will be entitled to claim for financing charges attributable to delays over and above outstanding payments, loss of profit and costs involved in demobilization (the last including claims from suppliers and sub-contractors less cost of normal demobilization).

PAM Form allows at clause 26.1(i) for termination by the contractor in the event of non-payment within the duration for honouring certificate **and**

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<sup>6</sup> Please see *Freeth v Burr* (1874) LR 9 CP

<sup>7</sup> At paragraph 4.221

after serving a notice to pay within seven days. Therefore in theory it is possible in the case of a contract with a 30 days' payment duration to be terminated after 37 days. Not surprisingly the PWD Form does not allow for termination by the contractor under any circumstances. The FIDIC Form carries very weighty provisions at clause 16.2 against the Employer which permit the Contractor to terminate the Contract in the event of delay in certification (paragraph (b)), and delay in payment (of 42 days after due date for payment, at paragraph (c)). FIDIC also permits termination by the contractor in the event that the employer is unable to provide evidence of satisfactory financing arrangements for the works.

### **3.2 Employer's obligation to allow the contractor to carry out the works without hindrance**

It is obvious that an employer must at all times permit his contractor to carry out his works so as not to delay his contractor from completing within the contracted duration. Failure to do so will result in the contractor ceasing to be bound by the contracted duration thus setting the completion date at large unless the contract allows the employer to extend the date for completion so as to permit the employer to recover liquidated damages in the event the contractor fails to complete by the extended date.

It therefore follows that a contractor has main two headings of claims in the event that an employer fails to allow the contractor to carry out his works unimpeded:

- i. To have the completion date extended so as to avoid liquidated damages (with the employer being left to his own devices to handle the delay which he must accept); and
- ii. Costs incurred by the contractor as a result of the delay.

We will examine each of the above in turn:

### **3.2.1 Delays and extensions of time**

It needs to be noted that all forms of contracts permit the date for completion to be extended for causes of delays (“neutral causes”) in addition to those caused by the employer (this includes those caused by his contract administrator, i.e. the architect, engineer, S.O., etc). Delays to sections of works entitle the contractor to extensions of time in their regard in the same manner as for delays to the whole works.

The following are neutral causes recognized as entitling completion date to be extended (PAM at clause 23.7, PWD at clause 43, FIDIC at clause 8.4):

- i. Exceptionally inclement weather (all three forms). This means that the weather for the time of the year has to be compared against that for the corresponding period during previous years. The norm is to compare the rainfall against the top say 5% highest recorded during a preceding few years (usually five or ten years)
- ii. Unforeseeable shortages of personnel or materials (FIDIC, PWD in respect of materials only)
- iii. Governmental actions although what this means exactly is not defined. How about action of a foreign government such as that of USA which has imposed sanctions on another country? (FIDIC only)
- iv. Strikes and lockouts. PAM recognizes this as a basis even if the impact is on the production of materials and equipment used on the works whereas PWD allows only for trades involved in the works.

As the above causes are of a neutral nature, whilst the contractor can claim time, he cannot claim to be compensated for the costs.

### **3.2.2 Delays and Costs**

*Generally* - all three forms of contracts allow the contractor to claim both for time for completion to be extended and costs incurred as a result of the delay. The two local forms contain clauses which expressly list the situations when the contractor can claim for delays caused, whereas FIDIC does not distinguish costs (defined in clause 1.1.4.3 to essentially cover expenditure and overheads) incurred in delays from costs incurred in overheads in for example carrying out variations. The contractor's entitlement is recognized in individual clauses addressing various issues. Thus, if the carrying out of a variation requires the contractor to mobilize, say, an extra crane and it is not convenient to include this in the rates, it will be recognized as a "Cost" together with the additional overheads incurred in the delay and prolongation (clause 13.3). Other instances of entitlement to costs which may involve delay costs is that incurred in opening up for inspection of works already covered up and which shows the relevant works to be compliant. In fact FIDIC expressly preserves the contractor's rights to claim at law (clause 20.1). This therefore allows the contractor to claim for costs involved in circumstances not specifically recognized in FIDIC but which would otherwise comprise rights at law such as for example as a result of disputes with neighbouring owners (recognized for example at clause 43(c) of PWD Form).

*How to claim and what are claimable –*

- i. in order to be entitled to claim, the first thing to do is to scrupulously notify of the intention to claim as otherwise the right may be lost<sup>8</sup>.
- ii. The question must be asked in respect of any item of claim "was this incurred as a result of the delay?". In other words and as an example, if

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<sup>8</sup> As in *Jennings Construction Ltd v Birt (Q.M.) Ltd* [1987] 8 NSWLR 18

a project involves say three blocks of buildings, of which one is delayed by four months due to the contractor's own default and another block is delayed by six months due to delay by the architect in providing details, most of the site overheads for four months will not be claimable. This is because they will be a need for site establishment to be maintained for the four months regardless of the delay in the receipt of information. Only two months' full site overheads will be claimable as these will not be incurred had there been no delay in the receipt of the information.

- iii. Anything else which would not have been incurred had there been no delay. This will include the escalation of materials cost. This right needs to be distinguished from "no price fluctuation" clause as such clause merely restricts the contractor from claiming had there been no delays caused but not otherwise. The claim is to be evaluated by tabulating the materials usage based on the programme after adding the effect of the delay and applying the relevant rates over the whole duration and subtracting from this the total cost based on the approved programme.

### **3.3 Contractor's claim for variations to the contract works**

The contractor is required to construct the contract works to comply with what the contract spells out, which has been dealt with at some length in 2.1.1 by the giving of examples. Therefore, if a contractor is required to carry out works which are additional (c.f. that which is outside in which case the contractor is entitled not to comply with the instruction) to those spelt out in the contract (normally included in the specifications and

drawings), then the contractor is entitled to additional payment. There are five points to note in this respect, i.e. on how the variation is to be evaluated:

- i. Based on the rates in the contract where the additional works are identical to those already included in the bills of quantities (PAM, PWD, and FIDIC);
- ii. Based on the rates in the contract but with an adjustment to reflect the fact that the work “may not be executed in similar conditions” to those in the contract (PAM and PWD). FIDIC contains arguably similar provisions but is worded differently. Thus for example, if the details of certain windows in a building are changed in that the rubber sealant is to be of a higher quality, then the same composite rate per window shall be changed to reflect the additional cost of the new sealant. As such, if an item has been underpriced, the same underpricing shall affect the new rate;
- iii. If none of the existing rates are applicable, the contractor will be entitled to completely new rates based on dayworks rates (as in the contract if available otherwise as per actual) the actual cost to the contractor plus 15% (PAM and PWD) or actual cost plus reasonable profit (FIDIC); and
- iv. If the varied works are such as to substantially affect the final contract sum, then the contractor is entitled to have the impact of this taken into account in determining the applicable rates.

It is pertinent to note that if the additional works instructed are outside the scope of the contract in either the nature of the works (such as for example substantial earthworks to a building contract) or physical limits of the contractor, the contractor is entitled to refuse to carry out the new works. Furthermore, even if the contractor wishes to carry out the works, it is strongly advisable that confirmation by the employer itself is obtained as

*Lim Eng Chong – 6 November 2008*

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the S.O./architect/engineer is not empowered to vary the contract (as against vary the works). In such a situation the contractor is also entitled to agree to the applicable rates and terms before proceeding.