HUDSON'S Building and Engineering Contracts

Eleventh Edition
First Supplement

By I. N. Duncan Wallace

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HUDSON'S

BUILDING AND ENGINEERING CONTRACTS

Including the Duties and Liabilities of

ARCHITECTS, ENGINEERS AND SURVEYORS

ELEVENTH EDITION

FIRST SUPPLEMENT
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INTRODUCTION

The Eleventh Edition of Hudson was published in 1995 in two volumes totalling some 1,700 pages. That expansion in size only partially reflected much earlier post-War developments prior to the Tenth Edition's publication in 1970 in general contract law and the very important (and at that time new) arrival of *Anns* and *Hedley Byrne* areas of liability for economic loss in tort. That earlier period had also seen the rapidly accelerating and inflationary growth of post-War construction and hence of construction litigation in all jurisdictions, and the proliferation of (increasingly complicated) standard forms as producer influences on those forms flexed their muscles, beginning in England with the 1963 family of the RIBA/JCT forms. The increased size of the Eleventh Edition also, of course, reflected the continuing and later influence of increasingly enthusiastic and innovative arguments by expanding producer-claims lobbies in both the building and civil engineering industries following the Tenth Edition in 1970, including the most recent 17-year period since the 1979 Supplement to that Edition (the latter, of some 50 pages, consisting of little more than case references in abbreviated form).

Notwithstanding the comparatively short period of eight years since the Eleventh Edition, the present Supplement is far more substantial, extending to 330 pages of text and references considered necessary to respond to what has very recently become a torrent of case law and of innovative changes in standard form contracts and contracting arrangements—the latter primarily designed (through promotion of so-called "management contracting" and the use of design-and-build concepts) to eliminate the post-contract administrative and supervisory services and control over interim payment previously exercised during the construction period until final completion by owners' original professional A/E design advisers, as well as to ignore or obscure the inherent and unavoidable differences (and in a construction contract context conflicts) of interest as between owner and contractor in areas of design suitability and quality. For producers there has also been the additional commercial attraction that these latest initiatives, if adopted, would make still more difficult,

if not impractical, accurate or useful price comparisons or indeed any form of realistic competitive tendering, thus prejudicing any effective value for money assessment by private or public owners at the contract stage.

It seems doubtful whether modern legal practitioners are aware of how revolutionary are the legal consequences of the changes in contracting arrangements which these sustained producer pressures have been increasingly advocating and which today often appear to be taken for granted. During the initial period before and after the Tenth Edition the comparatively limited expansionary focus of construction claims lobbies had been confined to the building industry in England, the objective being to promote wholesale remeasurement contracts using Bills of Quantities (though significantly according contractual priority to that industry's quantity surveyors' institutional Standard Method of measurement) for all but the most modest projects. This campaign was in fact surprisingly successful, particularly in the public and local government procurement domain, notwithstanding the large superstructure element in building projects, which should mean that final as-built quantities can be "taken off" the drawings and estimated with sufficient ease and accuracy at the pricing stage, leaving only a relatively small proportion of foundation or excavation work below ground level where, for practical physical reasons (and on some projects only) ultimate as-built differences may sometimes be sufficiently unpredictable to justify a remeasurement policy in the owner's as much as the contractor's interest (but for which in any case provisional sum or provisional quantity items or arrangements should be perfectly satisfactory without wholesale remeasurement of the entire project). Moreover, the words of incorporation in the standard forms, as well as those of the Standard Method itself, had been carefully crafted to permit highly ingenious and artificial "omitted item" claims for additional payment bearing little or no relation to site or pricing realities, and which could even permit substantial financial claims in cases where little or no change in the final as-built quantities outcome had as a fact occurred. Additionally, contracts using Bills of Quantities offer special opportunities for ingenious price manipulation or "unbalanced bid" techniques by pricing parties who have detected errors in the Bills or who are willing or able to take a view at the pricing or tender stage of ultimate as-built quantities or variation outcomes.

Quite apart from this special exposure to unjustified claims and artificial price manipulation, remeasurement contracts can be of benefit to professional advisers generally by disguising premature entry of the client into an inadequately pre-planned contractual commitment, so permitting earlier recovery of professional fees (though not, of course, without a corresponding loss of budgetary control over the final cost outcome), while conversely, under the then stringent public budgeting and annual expenditure controls, premature access to public funds for an insufficiently pre-planned project could be politically attractive to some classes of public owner.

Whether these unattractive features help to explain the surprising acceptance of these remeasurement contracts in the public building sector prior to the Tenth Edition must, however, remain a matter of opinion.

A second principal focus of producer pressures during this earlier post-War period (applying to both building and civil engineering contracting) had been the promotion of design-and-build contracts, in spite of their inherent unsuitability for competitive tendering and their often confused and inadequate draftsmanship (resulting from producer objections) to owners' design and suitability contractual entitlements if justifiably expressed (in the light of the inherent conflict of interest) in unconditional terms. By the time of the Eleventh Edition, however, while the pressure to promote remeasurement contracts as such now seemed (no doubt in the light of its earlier success) to be, at least nominally, reduced, it is evident that even remeasurement contracts were now being seen as objectionable with their single owner-supplied design permitting relatively easy price comparisons and their continuing role for owners' A/E advisers until final completion, so that new pressures became even more ambitious.

Thus Latham was in 1993 (some two years before the Eleventh Edition) openly recommending that professional firms of A/E advisers should be regarded at best as designers, to be dismissed altogether as soon as the initial design was complete, and that all their subsequent professional services (such as remaining design services, selection of contract documentation and contractors, and supervision and administration of the contract until final completion and payment) should instead be carried out by a new and admittedly restricted and privileged class (see the Egan Report) of major "management contractors", employed in an entirely new role (using a rather coy semi-professional description) as so-called "project managers". The design suitability and value-for-money dangers for owners of design-and-build contracting were now even greater, since the new project management arrangements envisaged that any continuing post-contract design services would be carried out by professional designers employed *not by the owner but by the management contractor*, often leaving in doubt for whom and in whose interest these design responsibilities (whether in contract or tort) were to be discharged.

Meanwhile, Latham's principal procedural recommendations, expressly designed to secure early payment of disputed interim claims and to override and replace the certifying and supervisory decisions of those A/Es whose owner-clients were still resisting the management contract concept, were in 1996 implemented by that year's HGCR legislation, requiring statutory mandatory adjudication by a class of adjudicator inevitably unfamiliar with the original design requirements or previous history of the project, but nevertheless required to reach major decisions on defence or set-off against disputed payment claims within extraordinarily short time limits. In addition, special one-sided (as between the parties) time limits invited

"ambush" tactics by parties able to prepare complicated and massive interim claims without any time or notice limitations, while imposing very short and unrealistic time limits for the submission of adequate defences or set-off against those claims by respondent parties. This was, of course, the regime created by the oddly-titled Housing Grant Contracts Regeneration Act 1996 and its detailed subordinate Scheme, which from 1997 will govern the great majority of construction projects and their associated professional contracts.

Reverting to management contracting, most available English standard forms unsurprisingly seek to reduce or qualify the management contractor's responsibility for the defaults of all the so-called "works contractors" operating, whether as sub-contractors or not, under the umbrella of the head management contract. To this must be added the effect of current Treasury PFI and PPP initiatives, where 30-year-long operational or maintenance obligations have been (often artificially) injected into the contract with an obvious consequence (by reason of their resulting rental or periodical pricing arrangements) in rendering separate pricing or segregation of a project's capital construction costs not only almost impossible to achieve but even officially and administratively "off-budget", thus increasing still further the difficulties of value-for-money assessments and reducing competitive price disciplines.

Finally, in the particular context of the contractor-inspired (though now in the light of the Latham and Egan reports semi-official) campaign to replace or diminish the influence and role of owners' A/E advisers and the advantages of competitive tendering, an additional more strictly legal argument is currently being advanced on behalf of contractors. This asserts an *affirmative* duty of care in tort owed by A/Es *to the contractor* when performing their whole range of duties of design, contract preparation, supervision, certification and administration under the terms of the construction contract itself, notwithstanding any conflict with their parallel professional obligations in contract to their owner clients. This argument not only seems wrong in principle, in view of the obvious conflict of interest involved as well as the alternative remedies available to contractors against owners under the terms of almost all construction contracts, but flies in the face of the clearly contrary authority of the Court of Appeal's persuasive reasoning and judgments in *Pacific Associates v. Baxter*, illustrated and discussed at very considerable length in the Eleventh Edition (see for the Editor's response to these latest arguments and more recent home and overseas cases, "*Pacific Associates* Re-Visited" in (2003) 19 Const. L.J. 303).

The fundamental, if not revolutionary, legal significance of current proposals, if the foregoing analysis is accepted, stems from the fact that (apart from reasonable-price jobbing contracts) all preceding Editions of Hudson and discussions of construction law since the First Edition at the end of the nineteenth-century have been principally directed at the interpretation of fixed price (in the special legal sense) contracts to carry out and complete defined work designed by

the owner's professional advisers for a fixed or ascertainable price, with interim valuation and payment initially regulated by the owners' A/Es as certifiers. As a further refinement on price, as previously explained, "schedule" or remeasurement contracts have been widely used for projects where the extent of the ultimate as-built work may for technical reasons be difficult to predict, so rendering accurate fixed pricing impractical at the time of tender. Thus remeasurement contracts had from quite early times become the norm for many civil engineering projects (as opposed to building contracts where sufficiently accurate estimated quantities for pricing of superstructures from the original drawings would be feasible, thus permitting the use of fixed price lump sum contracts, adjustable only for post-contract variations). Both types of contract, however, were compatible with competitive tendering and price comparison, and both equally recognised the obvious convenience and advantages of using the same A/E professional firm, which had originally produced the design in response to the client's amenity and cost requirements, to carry out the later day-to-day supervisory and certifying services required during the construction period. Commercially very importantly, these latter functions would include deciding disputes over defective work or alleged variations, and thus highly relevant to disputes on interim payment and valuation, over which the original A/E designers would be particularly well qualified to decide. Thus the most recent industry initiatives advocating management contracting, already supported by the officially commissioned Latham and Egan reports by the time of the Eleventh Edition, not only ignore but are directly opposed to fully justified construction owners' budgetary and value-for-money commercial interests in competitive tendering, as well as in safeguarding their quality and amenity contractual entitlements. These initiatives, therefore, seem inconsistent with the essential legal matrix and commercial objectives which govern the entire preceding corpus interpreting construction contract law, whatever policy judgments may be reached as to their desirability from the immediate point of view of consumers, tax payers or private or commercial construction owners as a class.

Contents of Supplement

Turning to its content, the text of this Supplement deals relatively extensively with a surprising number of legal problems of topical interest which have surfaced in the claims-dominated atmosphere of the construction field since 1995. In the field of tort, these include the surviving problems of economic loss and "complex structure" in the wake of the *Murphy* reversal in England of the *Anns* economic loss liability of developers, building and designers for defective buildings to later purchasers, as well as the arguments, previously mentioned, to establish an *affirmative* as well as a conventional *Hedley Byrne* and *negative* economic loss duty of care allegedly owed by owners' A/Es to contractors when performing their normal duties on behalf of their

clients prior to or under the terms of the construction contract itself. In the *Anns* context, care has been taken to draw attention (as in the Eleventh Edition) to a tendency, in all jurisdictions, to ignore site realities and the inevitable covering-in of all construction work and to assume an unrealistic degree of success by professional supervisors or inspectors in detecting or preventing (and so excusing liability in tort for) defective work or other failures of performance by developers, builders or designers.

Also in the field of tort, insufficiently considered and potentially damaging legislation has, it is submitted, been recently enacted in some Australian jurisdictions with the object, clearly demanded by producer and producer-insurance lobbies, of substituting a reduced proportionate liability of every individual construction industry defendant for the preceding one hundred percent *in solidum* liability of all defendants, whether severally or jointly liable with others and whether in contract or tort, laid down by previous contributory legislation in all jurisdictions. It is true that this proposal had also reached the stage of an earlier draft Bill in England, but the latter currently seems to be on indefinite hold, it may be speculated as the result of justified second thoughts (see the obvious anomalies and criticisms of this change on policy grounds as protecting and encouraging contract-breaking in a supervised construction context expressed by the Editor in CCPP Volume 2, Chapters 10, 11 and 12).

There has also been the problem of important new legislation in contract. In England this has involved two major 1996 enactments which overtook the Eleventh Edition, respectively the Housing Grants and Arbitration Acts of that year. As to the first, since that Act was essentially procedural and designed to afford temporary interim payment remedies to contractors against owners while postponing final resolution of their disputes until later arbitration or litigation, the view has been taken, in the light of a host of reported cases, that the principal substantive question requiring comment in Hudson concerns the enforcement in the courts of erroneous or unfair decisions or assumptions of jurisdiction by adjudicators under that Act. In regard to arbitration, the policy of the Eleventh Edition has been continued by attempting to discuss the new Act's practical consequences across the broad field of construction disputes—not an easy task at this very early stage following a self-styled re-statement of the entire law of arbitration.

In the field of contract proper (or under the new concept of concurrent liabilities in contract and tort) subjects dealt with in some detail include:

(a) The true measure of damage suffered by owners (or their lenders) following a negligent survey.
(b) Cost to the original builder (as opposed to cost of repair) as a more reliable measure of damage where defects causing loss of amenity only are present (see *e.g.* the *Ruxley* case).
(c) "Collateral compensation" or "no loss" cases (see *e.g.* the

Panatown case) where defeated contract expectation or "loss of performance interest" seems a valid but as yet relatively unexplored basis for liability in damages under English law.

(d) The causation difficulties and fallacies invalidating currently fashionable "concurrency" arguments in EOT or disturbance compensation disputes.

(e) So-called "global" or "total cost" bases for presenting compendious and unparticularised delay or disturbance claims.

(f) The related and increasing practice of using sums paid in settling third party claims as a basis for recovering similarly unparticularised damages by invoking the *Biggins v. Permanite* principle.

(g) The abuse of approved programme provisions (with related arguments justifying removal of their "float" element) in place of the stipulated contract completion date so as to advance time-related obligations of owners and increase the quantum of delay or disturbance claims.

(h) The haphazard effect of a contract's "works" insurance provisions in excluding contractor or sub-contractor liabilities in contract or tort.

(i) The correct use of formula-based claims for lost "fixed" overheads recovery on delayed contracts.

As is evident, the above questions derive their origin from the fertile territory of contractors' claims lobbies.

The previous policy of Hudson, in endeavouring to explain the practical background and competing commercial interests and objectives underlying construction contract provisions or case law in some detail for the benefit of legal students or practitioners coming to the subject for the first time, while correspondingly seeking to explain legal concepts and decisions at some length in terms understandable to readers without legal training, has been continued, as also the use of illustrations.

While the increase in construction litigation and specialist reporting in all jurisdictions and the new techniques of global electronic retrieval have combined to produce a massive and now almost unmanageable increase in the data-base previously covered by textbook writers, the attempt to notice at least those developments in overseas common law jurisdictions which assist the evolution of a coherent general philosophy of interpreting construction contracts has been continued, though readers' indulgence is requested for inevitable lapses in the comprehensiveness of this cover. This increase of data-base seems likely to pose fundamental problems for future generations of legal textbook writers, particularly in those specialist areas of law where practitioner as well as academic experience is thought to be of value.

TABLE OF CASES

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