

Valuation of variations under JCT standard forms of contract (or 'THE DYING ART OF FINAL ACCOUNTING')

This briefing gives DAQS' view of the interpretation and application of the rules for valuing measurable variations embodied in the JCT 1998 and 2005 Standard Forms of Building Contract ('JCT 2005' and 'JCT 1998').

In fact, as the Guide to JCT 2005 at para.66 confirms, no material amendments have been made in JCT 2005 in relation to the basis of the Valuation Rules set down in JCT 98 and therefore JCT 2005 and JCT 1998 have essentially been considered together for the purposes of this briefing.

INTRODUCTION

All too often, disputes over adjustments of the Contract Sum occur between contracting parties (whether commercially or in adjudication, arbitration or litigation) in the operational part of the construction chain, i.e. Employer/Contractor and Contractor/Sub-Contractor. Those disputes are usually artificially widened or exacerbated by the

reluctance, or refusal of the QS, and/or the Contractor and/or the Subcontractor to understand and properly apply the rules set down in the respective contracts for the valuation of the execution of additional or substituted work, or for dealing with Approximate Quantities in the Contract Bills. Instead, the parties involved in valuation often prefer, or agree, or acquiesce to 'dumping' the valuation dispute into the loss and expense claim, generally on the basis that they cannot agree what constitutes dissimilar character and/or conditions, or what is a fair allowance or a fair valuation. It appears that they convince themselves that the resolution of their differences lies in the evidencing of actual cost and should therefore be dealt with under the loss and expense claim.

This is not only a problem confined to the JCT Contracts which are the subject of this briefing, but also extends to most

other standard forms of contracts and subcontracts which contain provisions for recognising that adjustments should be made for variation work of dissimilar character and/or executed under dissimilar conditions; and significant changes in quantity.

THE VALUATION RULES – JCT 2005 AND JCT 1998

It is helpful to consider the rules in the form of a basic cascade chart as shown at figures 1 and 2 below:

QUANTITY SURVEYOR'S ROLE

The QS is given the sole obligation under the Contract to value additional or substituted work which can be properly valued by measurement, and also to measure and value work for which an Approximate Quantity was included in the Contract Bills, in accordance with the rules set down in the Contract.

ADDITIONAL OR SUBSTITUTED WORK

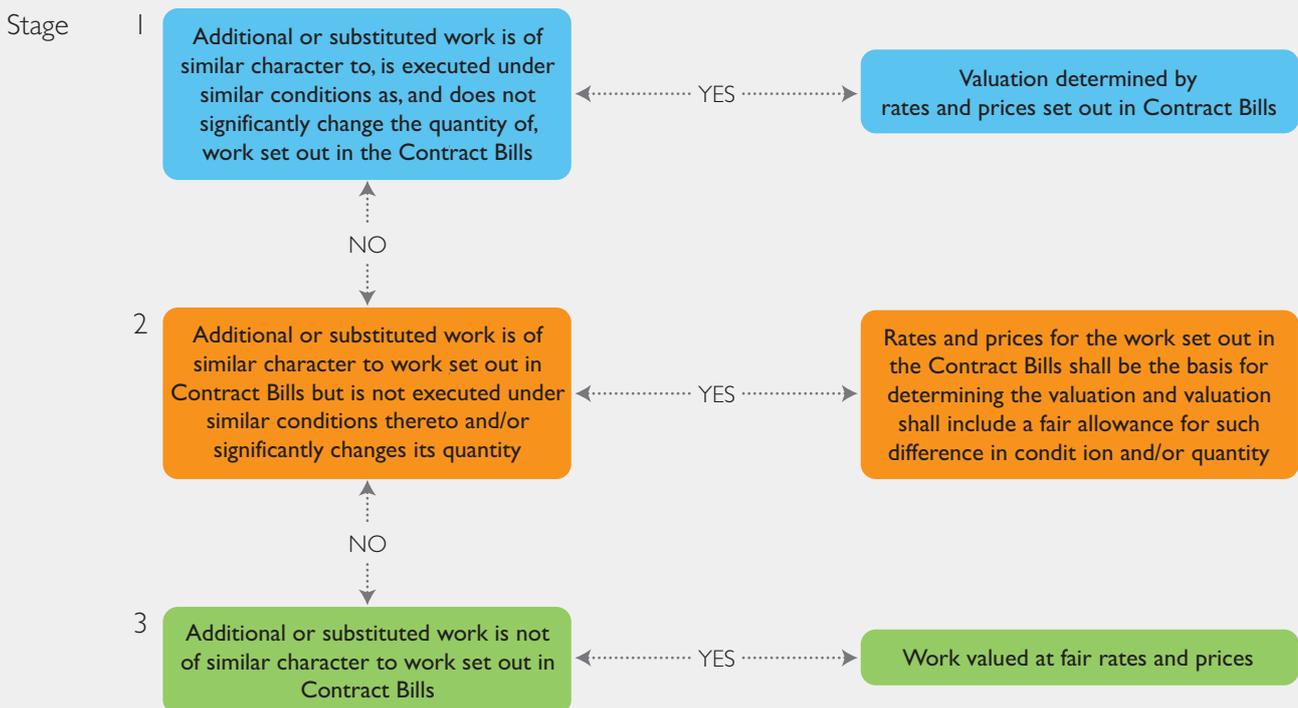


Figure 1

APPROXIMATE QUANTITY INCLUDED IN CONTRACT BILL

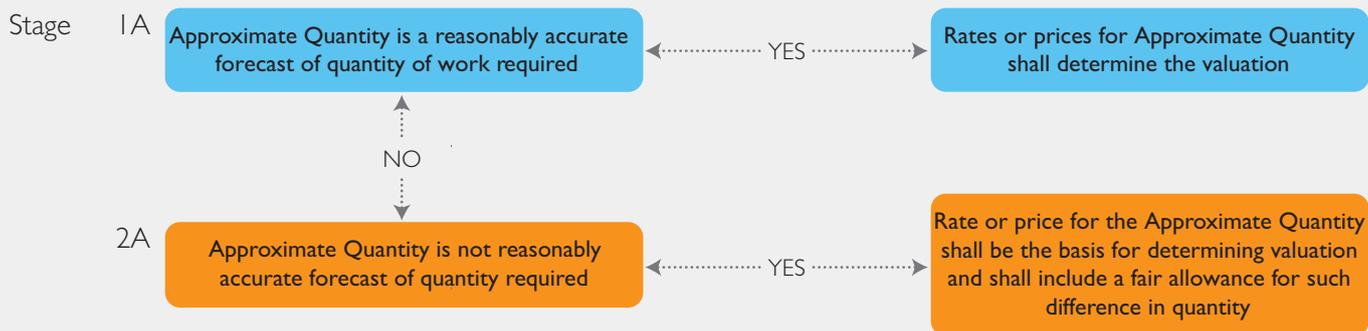


Figure 2

The Contractor has the right to be given the opportunity to be present when it is necessary for the QS to measure work for the purpose of Valuation.

Although likely to be paid by the Employer, the QS has express obligations to act fairly in applying the Valuation Rules by exercising his professional judgement to arrive at a fair allowance for additional or substituted work not executed under similar conditions to those set out in the Contract Bills, or for determining a fair valuation where the work is of dissimilar character (see Fig. 1). The Employer has contracted with the Contractor that the QS will act fairly and professionally where the Rules expressly require him to do so.

SIMILAR CHARACTER AND CONDITIONS

If, as Stage 1 of Fig 1 illustrates, the additional or substituted work is of a similar character to work set out in the Contract Bills; is executed under similar conditions from those which can be derived from the Contract; and does not significantly change in quantity then the Bill rates must be used in its valuation by the QS irrespective of whether or not the rates in the Bills are overpriced or underpriced; and irrespective of actual costs incurred.

DISSIMILAR CONDITIONS

The starting point for Stage 2 of Fig 1 is that the additional or substituted work is of similar character to, but the conditions under which it is executed are different from the work set out in the Contract Bills. An example of this would be where it can be established that the Contractor's rates in the Contract Bills for external cladding were

estimated on the basis that all the cladding work would be carried out in summer; but additional cladding of the same type was instructed which had to be carried out during the winter period.

The work here is of similar character but the conditions under which it is executed differ from those anticipated in the Contract Bills. Therefore, an adjustment to the Bill rates should be made by the QS by way of a fair allowance.

So far as changes in physical conditions are concerned, Keating on Building Contracts Seventh Edition in commentary on the Valuation Rules in JCT 1998 gives a number of examples where physical site conditions may differ:

- Wet compared with dry
- High compared with low
- Confined space compared with ample working space
- Winter working compared with summer working

In terms of making an allowance which is "fair" (which must mean fair to both parties), the question is already answered by the allowance being made on the basis of the contract rates. Therefore some form of percentage uplift to the contract rates could be contemplated. In these cases, the QS could consider market rates, not in themselves, (Contract rates are to be adjusted), but to decide how to adjust the Contract rates to take account of the dissimilar conditions. Standard rates can assist. For example, if a contract exists for construction of a brick bungalow, and additional brickwork one level higher is instructed, then the QS can look to, for example, Wessex to see what height factor

could be applied to conventional rates in such circumstances. That factor could be applied to the original contract rates and prices. Thus a fair allowance takes into account the market view of what is a fair adjustment for dissimilar conditions prevailing but only applies it to the contract rates. That is "fair" because it maintains the contract basis whilst taking an objective view of the allowance to be made. Therefore, if the Contractor had underpriced the brickwork rates, then it would get no relief from those underpriced rates, but would recover only the effect of the dissimilar conditions.

DISSIMILAR CHARACTER

If Stages 1 and 2 of Fig 1 do not apply and the additional or substituted work is established to be "not of a similar character to work set out in the Contract Bills", then Stage 3 of Fig 1 applies with the work being valued at fair rates and prices. It is again suggested that "fair" means fair to both parties, i.e. in the context of the contract between the parties.

Take, for example, a brick faced multi-storey block, where the facing bricks are specified as wirecut, of completely regular size, shape and colour and laid with a flush joint.

A variation is instructed to change to handmade rustic facings laid with a recessed joint, together with a stringent specification requiring colour, shape and size brick selection within strict tolerances and from several packs concurrently. This, of course, would be likely to lead to a situation of high wastage and low productivity by bricklaying gangs.

How, therefore, should the QS fulfil his obligation to arrive at fair rates and prices in applying Stage 3 of the Valuation Rules at Fig 1?

No reference is made in the Rules to evidence of actual cost being a valuation factor; nor is there any express reference

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to the Contractor having to keep records to underpin the QS' judgemental valuation. Yet it would clearly be in the Contractors' interests to produce invoices for the purchase of the varied bricks (which probably form 60% of the variation rate), calculations of wastage, and 'measured mile' records of labour productivity. Armed with this information and his own professional judgement, the QS should be able to arrive at a fair rate for the variation.

On the other hand, it may be dangerous, for instance, to take the Contractor's actual labour costs as evidence of reduced productivity because the Contractor may not be able to engage sufficient bricklaying gangs of the right skill level to cope with the increase in quality of the facing brickwork or have adequate bricklaying supervision on site.

At the end of the day, the obligation to arrive at the fair rate is with the QS and even in the absence of information from the Contractor, the QS must still hold the ring between the Employer and the Contractor and, use his professional skill and judgement to arrive at a fair valuation. What the QS cannot do, provided there is no dispute as to whether the variation has been executed, is to refuse to fairly value the variation in the absence of information from the Contractor.

If this cannot be achieved then the Contractor may have a valid argument that the variation is priced at daywork rates or the loss is dealt with as loss and expense, in which case there is some justification for keeping actual cost records of the direct cost of variations.

PRELIMINARIES

The 2005 and 1998 Valuation Rules for measurable work as reflected in the above cascade charts require the QS, in making a valuation under the rules to make...

"allowance, where appropriate... for any addition to or reduction of preliminary items of the type referred to in the Standard Method of Measurement (SMM)."

Therefore, in making a valuation relative to any of the Stages illustrated in Figs 1 and 2 above, the QS is obliged to establish whether any of the types of Preliminaries items given in Section A of the SMM should appropriately be the subject of an allowance in the valuation.

For instance, an Architects Instruction to construct an additional internal block, wall 30m long x 3 m high would require a number of the types of Preliminary item

given in Sections A40-A50 of SMM 7, e.g:

- Management staff to set out and supervise
- Scaffolding
- Distribution of blocks and mortar to worksite location
- Clearing away of waste and rubbish
- Protection of adjacent work

In making the allowance the QS is not bound to using the rates and prices for Preliminaries in the Contract Bills; nor can he insist upon evidence of additional costs incurred; or records to evidence the resources used.

Once he decides that the types of item are appropriate, he is bound to use his professional skill and judgement to arrive at the allowance. This, of course, recognises that there may be some duplication with time and/or disruption elements in the loss and expense claim which would require adjustment within that claim. Further, the Valuation Rules at clauses 5.10.2 of JCT 2005, and 13.5.7 of JCT 1998 expressly prohibit any allowance being made by the QS *"for any effect upon the regular progress of the Works, or of any part of them or for any other direct loss and/or expense for which the Contractor would be reimbursed under any other provision in these conditions"*.

The above clauses only apply to the extent that payment has been included elsewhere, i.e. by way of Clause 4.23 of JCT 2005 and clause 26 of JCT 1998. This does not mean that valuation of related preliminary cost under the Valuation Rules is a secondary approach to finding out the loss/and or expense under clauses 4.23 and 26. Clause 5.6 of JCT 2005 and 13.5 of JCT 1998 are about value. Clauses 4.23 and 26 are about cost. Both of these clauses are subject to notice provisions, whereas the Valuation Rules reflected in clause 5.6 and 13.5 are not.

The QS has to apply himself to preliminaries in the same way as other aspects of valuation under clause 13, i.e. the starting point may be the rates included in the Contract Bills, so for instance if variation to include painting causes the project to be extended by 4 weeks what is the difficulty in using clauses 5.6.1.3 of JCT 2005 and 13.5.3.3. to value preliminaries?

IMPACT OF VARIATIONS ON NON-VARIED WORK

The most under-used and under-considered of the Valuation Rules are the provisions clause 5.9 of JCT 2005 and 13.5.5 of JCT 1998 which require the QS where the instruction of a variation results in other work, not itself varied, being executed in conditions other than those which are to

be derived from the express conditions of the Contract.

Take for instance a variation to change the external cladding of standard profile and standard sheet sites, and which could be installed from an access scaffold, to complex rainscreen cladding in non-standard sheets with every sheet site measured, and which requires an independent scaffold tied through the building, considerably restricting access and working space for follow-on trades e.g. plastering. The change in conditions would make the plastering itself (where it was executed in such areas of restricted access and restricted working space) subject to the Valuation Rules, with the QS obliged to make a fair allowance for the difference in conditions.

The QS would also be obliged to make an allowance for preliminary items due to the change to independent scaffolding, and for any other preliminary items which may appropriately arise from the change.

This provision is a little used approach to the valuation of variations, with the parties involved often inclined to treat the effect on non-varied work as consequential and falling to be dealt with under the loss and expense claim but it does not have to be that way. The Valuation Rules are not constrained by notice provisions so in the absence of notice the Contractor should be able to show that the change is capable of being valued under the Valuation Rules.

2005 JCT STANDARD BUILDING SUBCONTRACT

The recently published 2005 JCT Standard Building Sub-Contract, SBSub, provides for two alternative approaches to measurement and valuation of Subcontractor variations, depending on whether or not Articles 3A or 3B are incorporated into the Subcontract.

Article 3A requires a Sub-Contract Sum to be inserted and variations to be made on an adjustment basis; Article 3B requires a Sub-Contract Tender Sum to be inserted in which case all the Sub-contract works are to be completely remeasured and valued.

The obligation to measure and value the adjustments or the remeasurement is upon the Contractor.

The rules for valuation of measurable work on an adjustment basis and a remeasurement basis in terms of "similar character" and "similar conditions" mirror those shown in Fig.1 on page 1.

CONCLUSION

It is clearly in the interests of the parties to both the main contract and the subcontract that the measurable or remeasurable final account is dealt with as fully as possible before they move on to attempting to resolve the more esoteric questions of liability and quantum relative to loss and expense claims.

To pave the way for subsequent valuation of loss and expense particularly in relation to disruption an analysis should be prepared that indicates the recovery of staff, equipment and labour in variations so that account and particularisation of them can be provided when ascertaining the loss and expense

The satisfactory resolution of the measurable or remeasurable final account is essentially a value-related exercise dependent upon the QS (and the Contractor in the case of the subcontract) applying the rules properly and making allowances and valuation which are fair to both parties, where he is expressly required to do so.

The application of the Rules is not a cost related exercise, although it is accepted that where a "fair valuation" is required, actual cost may be one of the strands of consideration, as would be, for example, market rates or text book differential productivity factors.

Whilst the Contractor and Subcontractor are not expressly required to give notice or keep records to underpin fair allowances and fair valuations, it clearly may be prudent for them to do so in some circumstances, e.g. to demonstrate productivity reductions from the factors contained in Bill rates.

It is also accepted that adjustments may have to be made to take account of duplicated recoveries, or overlaps in recovery, between the measurable final account and the loss and expense recovery, e.g. for staff. It is suggested that these adjustments are best made in the loss and expense claim.

Malcolm Trusler

ARE YOUR SYSTEMS IN PLACE TO DEAL WITH DELAY

Delay and whodunit? - an answer on a post card

A light-hearted and abbreviated but directional view of delay analysis.

This story is about three WHO's:

- WHO-1, WHO-2 and WHO-3.
- WHO-1 one in a contract with WHO-2.
- WHO-3 is the Contract Administrator.
- WHO-2 can affect WHO-1's progress and performance but so can WHO-3.

And now for the postcard: "WHODUNIT?"

Now some would say that for WHO-1 to achieve the above it is easier said than done.

However all WHO-1 has to do is find the common denominator in his focused RECORD keeping so that all information can be coded, allocated and retrieved.

Think of RECORDS as 400,000 pieces of paper in a 100 filing cabinets, easy to file but impossible to retrieve if a system is not in place.

Roy Pickavance

Dear ...

WHODUNIT - WHO-1, WHO-2 or WHO-3?

HOW TO FIND OUT

1. Have a PLAN
2. NOTE when WHO-1 is given an area of work by WHO-2.
3. NOTE what WHO-1 does, where, how much and in what time.
4. NOTE when WHO-2 prevents or interferes with WHO-1 doing what and where.
5. NOTE when WHO-3 prevents or interferes with WHO-1 doing what and where.
6. NOTE when WHO-1 hands back an area of work to WHO-2.
7. ALWAYS make these NOTES legible and in a format suitable for processing.
8. Process the NOTES, transmit them to WHO-2 as records, give notice to WHO-2 and show what would have been "BUT FOR" WHO-2's and WHO-3's actions or inactions.
9. OFFER alternative solutions to recover the project out of the ashes.

Regards
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