Lecture 1
Fundamentals of Contracts

Speaker:
Prof. Rizwan U. Farooqui, PhD
Professor and Co-Chair
Department of Civil Engineering
NED University of Engineering and Technology

Outline
- The Basics
- Elements of Contract
- Contract Design Considerations
BEGINNING OF CONTRACTS

END OF CONTRACTS
Condition of the Parties if the Contract was not Managed Efficiently or the Risk were not Managed Effectively!!

Project Over-budget, poor quality, delays, safety issues, unsatisfied client, disputes, litigation, loss of reputation, sore relations.
The Basics

Traditional Project Structure

- Multiple Parties
- Multiple Contract Types
- Varying Skill Levels
- Diverse Motives
- Gaps
- Hope
Why Contract?

The success of a project is largely influenced by;

- The accuracy and details of its documentation
- The understanding between parties, acceptance of their particular responsibilities and deliverance
- How professionally and accurately the day to day administration is handled
- How changes are dealt with?
- How conflicts are mitigated/ resolved.

What is a Contract?

- A construction contract is a legal agreement between two parties for performance by one party and payment by the other.
- The law recognizes performance and payment as duties and provides a remedy if one party fails to perform (i.e. breaches) the terms of the agreement
- The contract should state the work to be performed, the price, and when the contractor will be paid
- Contract determines what has to be done and how to compute time & compensation for work beyond the contract.
- The contract terms are critical in determining the rights and obligations of the parties in the event of a dispute
- If the issues are not spelled out, you must rely on provisions of applicable common laws or statutes
Elements of a Contract

1. An offer
   1. Must be clear, complete, and communicated
   2. It is valid for a “reasonable” duration
   3. Can be revoked prior to acceptance unless otherwise specified

2. An acceptance
   1. Must be absolute and unambiguous

3. Agreement
   1. There must be a meeting of mind
   2. A mutual mistake can allow either party to void a contract, but, unilateral error does not.
   3. Ambiguities are usually construed against the drafter of the document
   4. Fraud or misrepresentation may enable the victim to void the contract
Elements of a Contract

4. Valid Consideration
   1. Is the actual or promised exchange of money, goods, services, or some action or inaction

5. Between Competent Parties
   1. The parties must have valid authority to contract for their organization
   2. Unlicensed contractors may not enforce payment even if they have fully performed their obligations

6. Legal Form and Content
   1. Contract must conform to legal requirements. Contracts for actions that are illegal or against public policy are unenforceable
   2. Oral contracts and oral modifications to contracts are generally enforceable, but difficult to prove
   3. Most construction contracts require written authorization to perform extra work, which would generally negate an oral agreement or contract modification

Elements of Construction Contract Documents

1. Bidding Requirements
   • Advertisement/Invitation to Bid
   • Instruction to Bidders

2. Forms of Tender and Contract Securities
   • On a standard form, prepared by a design professional association or by the owner who frequently construct projects.
   • Bid Security Form
   • Performance bond form

3. Conditions of the Contract
   • Include the general and special conditions
Elements of Construction Contract Documents

4: Technical Specifications and Special Provisions
Describing material required, quality of workmanship, required procedures or techniques. Can be organized in levels:
• Level 1: Organization into divisions
• Level 2: Organization of divisions into sections:
  1. Scope: defines the work covered
  2. Materials: standards, brands, types, strengths, etc.
  3. Workmanship: means and methods, testing
  4. Measurement and payment: on unit price contracts

5: BOQs and Schedule of Prices

6: Drawings

Elements of Construction Contract Documents

7: Supplementary Data
  1. Soil reports and any special studies or tests included or referenced in the contract documents

8: Addenda and Contract Modifications (approved VOs)
  1. Addenda and pre-bid changes to the contract are issued after the bid docs are released to bidders but before bids
  2. Record approved changes on the plans and specifications and schedule of values Scope: defines the work covered
Characteristics of a “good” Contract

- Carefully considered
- Expressed clearly
- Time-tested
- Fair
- Balanced
- Applicable to the elements of a project
Contract Design

- Scope Definition
- Risk Sharing
- Variations
- Dispute Resolution
- Pointers to Avoid Disputes, Defend Contract

Fundamental Idea

- Structure contract so that
  - Risks that the contractor can handle better are imposed on contractor (i.e. contractor will lose money if don’t control - to be competitive, will have to manage these)
  - Risks that the owner can handle better are kept by owner
Fundamental Balance

- Impose *high enough risk incentive* to get contractor to do job efficiently and effectively within the specifications of the contract
  - *Owner provided Incentive*: E.g. Incentive to finish on time, incentive to stay within budget
  - *Contractor Response*: E.g. better resources, equipment provision, management support
- Impose *low enough risk* to have reasonably low bid

Advantages of using a Standard Form of Contract against a Bespoke contract

- Contractors aware of the risks, hence likely to be more competitive
- There are legal cases available for interpretation of the clauses. Hence post contract disputes are likely to be less.
- Each party is well aware of their risks and obligations and hence more chance of success.
- Changing the standard form of contract without good professional advice creates many ambiguities in the contract. E.g. If cost escalation clause is changed so as to disallow for any increase in prices but no clarification is incorporated for the variations, then it would result is many disputes.
- If provisions are altered in a Bespoke form of contract to align the contract completely in favor of the client, there is even a possibility that in case of any dispute, the court may even reframe the contract to make it more equitable or in worst case may even void the contract.
Questions, Comments?