

## KCRC Contract Strategy

KCRC contract strategy is founded on best Hong Kong and international practice, the principles of which are set out in –

- (a) Sir Michael Latham's Report, *Constructing the Team*, 1994 (Commissioned by the UK Government)
- (b) Sir John Egan's Report, *Rethinking Construction*, 1998 (Commissioned by the UK Government)
- (c) The Report of the Construction Industry Review Committee, *Construct for Excellence*, January 2001, chaired by Mr. Henry Tang (Commissioned by the Chief Executive of the HKSAR)

### Detail

The early 1990s saw a serious decline in the construction industries in both the United States and Britain. Although economic factors were the main cause of this decline, one other underlying factor was felt to be the industry's over reliance on the use of litigation and arbitration to settle disputes and claims. The UK Government commissioned Sir Michael Latham to lead a year long enquiry with the aim of ending *the culture of conflict and inefficiency that dogs Britain's biggest industry*.

The Latham Report, which was published in 1994, concluded that the industry's traditional methods of procurement and contract management and its adversarial culture caused inefficiency and ineffectiveness. The Report stated that addressing these issues had the potential for saving 30% over five years. The 30 recommendations made in the Report included making greater use of *alternative dispute resolution methods*. Indeed, the Latham Report made reference to the dispute resolution process used under the Airport Core Programme as an example of such an alternative approach. The KCRC developed its contract strategy for the West Rail projects in 1997. While standard conditions of contract adopted for West Rail were based on those used for the Airport Core Programme, by the MTRC and by the Federation Internationale Des Ingenieurs-Conseils (FIDIC), the principles and philosophy inherent in the strategy followed those of the Latham Report.

While the Latham Report was widely welcomed, implementation of its recommendations was perceived to be slow and as a result the UK

Government established the Construction Task Force, led by Sir John Egan. The Egan Report, "Rethinking Construction", acknowledged that its foundation was the Latham Report. The report found *growing dissatisfaction with construction among both private and public sector clients. Projects are widely seen as unpredictable in terms of delivery on time, within budget and to the standards of quality expected.*

The Report saw a need for a change of style, culture and process in the construction industry. To this end, it identified five "drivers" which needed to be in place to secure improvement in the construction industry, namely, *committed leadership, focus on the customer, integrated processes and teams, quality-driven agenda, and commitment to people.* Within these drivers the need for partnering and sharing of risk between contractor and client was identified.

The findings and conclusions of the Latham and Egan Reports are mirrored in the Report of the Construction Industry Review Committee, chaired by Mr. Henry Tang. The Report, Construct for Excellence, which was published in January 2001, made 109 recommendations. Amongst these were recommendations on selection of contractors, risk allocation, dispute resolution and partnering. [Copies of the Report may be obtained from the Works Bureau website <http://www.wb.gov.hk/archive/archives/review/report.htm>]

The recommendations of the Report are now being implemented by the Government. A Provisional Construction Industry Coordination Board has been established to take forward the recommendations in respect of the local construction industry. KCRC is represented on the Board in the person of the Senior Director, Capital Projects.

### Selection of Contractors

On selection of contractors, the Tang report stated –

5.29 *Except for complex, high value projects, public works contracts are normally awarded to the lowest tenderer provided that he satisfies all other technical requirements. Among eligible tenderers on the list of Approved Contractors for Public Works who possess the relevant technical competence, meet the financial requirements and have not been suspended from tendering as a result of adverse performance reports, the one offering the lowest conforming tender will normally be selected unless there are sound justifications for not doing so.*

5.30 *For public works contracts which are of a high value, complex and technically demanding as well as those contracts which are subject to a very rigid completion programme and require a high level of co-ordination, prequalification of tenderers is usually carried out. The use of prequalified tendering and the evaluation criteria require the prior approval of the Secretary for the Treasury on the advice of the Central Tender Board. While a marking scheme is normally used in the prequalification exercise, selection from among tenderers so prequalified is normally based on their price bids. No particular preference or weight is given to the tenderer whose past performance and quality attributes have been rated in the prequalification exercise as superior to the other tenderers.*

The Tang report went on to say –

5.35 *For major projects which have undergone the prequalification process, tender selection from among the prequalified tenderers is at present primarily based on price. In the spirit of the proposed quality-led approach to construction procurement, we recommend that quality attributes should also be taken into account in the tender evaluation process.*

#### Allocation of Risk

On allocation of risk, the Tang Report stated –

5.48 *Risks and uncertainty with potentially damaging consequences are inherent in all construction projects. Such risks include contractual, environmental, financial, economic, market, logistical, design, construction, and operational risks. Failure to manage risks effectively may lead to serious consequences, such as prolonged contractual disputes, programming delays and budget over-run. Effective risk management and equitable contracting arrangement provide the necessary tools to enable the contracting parties to achieve the project objectives to their satisfaction.*

More particularly, the Report noted that –

5.55 *In spite of allocation of risks through the contract, any significant default by the contractor remains the client's risk. It is, therefore, in the interest of both parties to adopt contracts based on an equitable allocation of risks.*

## Dispute Resolution

The Report proposed that a contract document should contain –

5.59 *... an effective means to settle disputes as risks materialize.*

5.60 *As a matter of good practice, the contracting parties should address all claims and potential claims as early as possible to prevent them from developing into disputes.*

5.61 *The resolution of disputes can be expensive and time-consuming. Given the substantial cost and disruption that a dispute may cause to a contract, the contracting parties should avoid disputes as far as possible.*

The Report went on to say –

5.63 *In the event that a dispute becomes unavoidable, it is important to manage it actively and positively to encourage early and effective settlement. Different procedures, such as negotiation, alternative dispute resolution (e.g. mediation, the use of a dispute resolution adviser and adjudication), arbitration and litigation, may be resorted to, having regard to the circumstances of a particular dispute.*

5.64 *Consistent with our overall objective of facilitating project delivery, we recommend that -*

- (a) *Employers, consultants and contractors should be encouraged to adopt a proactive approach, with sufficient high level support and involvement, to resolving claims and disputes as they arise. Training for the project team and other resources should be made available to ensure the effective implementation of this approach; and*
- (b) *Proactive and collaborative ways of dispute resolution should be encouraged through the adoption in contracts of provisions which facilitate the resolution of disputes by means of alternative dispute resolution techniques (such as the use of a dispute resolution adviser and/or dispute review board), in addition to formal and binding adjudication means which will remain a necessary, but last resort, solution.*

## Partnering

On the importance of partnering, the Report stated –

5.65 *Key participants in a project, including the employer, the designer, the engineer, the main contractor, subcontractors and suppliers, need to work together more effectively and efficiently to complete the project in a satisfactory manner.*

5.69 *We, therefore, recommend that public sector clients and progressive clients in the private sector, together with their project teams, should help to foster a new culture in the construction industry through more extensive adoption of a partnering approach in implementing their construction projects.*

5.70 *In the longer term, to provide a solid foundation for the project partnering process, we recommend that further consideration should be given to the integration of a partnering approach into the contractual relationship by developing a new form of contract that is based on co-operation, client focus and commitment to best practice for application to local construction projects. The C21 Construction Contract developed by the New South Wales Government in Australia and the ACA Standard Form of Contract for Project Partnering (PPC 2000) launched in the UK recently provide useful reference in this regard.*

5.71 *For other clients and project teams who do not feel ready to adopt the full structured framework of partnering, we recommend that they should seek to secure teamwork, good practice and commitment from all parties at a project level through a jointly developed project pact. In essence, the project pact establishes a framework of common values and expectations. It drives the project team to meet the needs and expectations of the client on the one hand, and the client to take necessary action to facilitate that outcome on the other. The agreed project pact should be distributed throughout the project team and displayed prominently wherever possible to serve as a constant reminder of the commitment of the project team to deliver a successful project.*