



CONTRACTUAL RELATIONS IN DESIGN AND CONSTRUCTION

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INTRODUCTION

This note provides a brief overview of contracts relating to the work of design teams. The design team members advise the employer on the cost and design of a building, will supervise its construction and will certify payments due to the contractor. Each of the roles involved require careful definition in order to minimise the potential for disputes.

1 ROLE OF DESIGN TEAM

The employer normally requires professional advice on the design of the works and the preparation of the contract for the execution of the works, from an **architect**, **structural engineer**, and **quantity surveyor**. The architect or engineer supervises execution of the works and certification of payments to the contractor.

The **architect's** duties normally include the design of the building, putting in place of contractual arrangements for the construction of the building, and the administration of the contract, including inspection of the works. The design element of the architect's work in a large building project generally refers to the amenity and functionality of a building, rather than the structural soundness of the building.

The design function relating to the structural soundness of the building project is carried out in a large project by the **structural engineer**. The **mechanical and electrical engineer** designs and oversees the works relating to services and electrical elements of the building project.

The **Quantity Surveyor** was defined in an 1870 case as a person

"whose business consists in taking out in detail the measurements and quantities from plans prepared by an architect for the purpose of enabling builders to calculate the amounts for which they would execute the plans"

The QS prepares an estimate of the cost of the works, prepares schedules for pricing by tenderers for the purposes of pricing variations in lump sum contracts, and assists in the negotiation and obtaining of estimates for work carried out by third parties. The QS also prepares the final account, including adjustment of PC sums, calculation of sums due under price variation clauses in the contract, etc.



CONTRACTUAL RELATIONSHIP

2 LETTERS OF ENGAGEMENT/APPOINTMENT

It is important to have a letter of engagement or appointment entered into between each of the design team members and the employer (or, in a design and build contract, the contractor). Typically these letters will deal with the following:

- Scope of services to be provided by professional;
- Standard of care to be exercised by professional;
- Supply of certificates or opinions on compliance with planning permission and building regulations;
- Professional indemnity insurance obligations, providing for a minimum level of cover and specifying the period during which this cover should be maintained;
- Fees payable to professional;
- Covenants by professional to provide additional documents on demand, such as collateral warranties and/or step-in agreements which I will discuss later.

Disputes can arise between professionals and employers where the arrangements between the parties in relation to the above matters are not documented with sufficiently clarity. In the area of fees, in particular, disputes can arise where additional services are undertaken by the professional which are outside the scope of the normal services provided. For example, where an employer requests a change to a design, this may necessitate considerable additional work and expense for the professional. A carefully drafted appointment will hopefully anticipate such additional works and will have allocated the cost of these works either to the employer or to the professional.

CR – standard forms

The following documents are the standard forms used for each of the design team members:

- **Architects**

The RIAI form of Agreement between Client and Architect for the provision of architectural services, 2002 edition, is the current industry standard form.

The agreement deals with the services to be provided by the architect, divided into 5 work stages. It then deals with charges, and contemplates that the charge should either be as a percentage of the total construction cost, defined as the cost of all the work including site development works, or by way of a lump sum fee.

The charges section also contemplates that an hourly rate for additional services should be included.

This hourly rate might apply, for example, where the client requests that designs which the client has previously approved should be changed, in accordance with Clause 7 of the terms and conditions.

So, it is necessary to decide whether the architect should be paid on a fixed-fee basis, or on the basis of a percentage of the total construction cost.



Finally the form sets out the terms and conditions of the agreement.

CR modifications

Some modifications that may be made to the RIAI standard form are as follows:

- Restrictions may be imposed on the authority of the architect, such as a provision that variations which may give rise to an additional cost to the employer may not be ordered by the architect without the prior approval of the employer.
- Professional indemnity insurance to be maintained by the architect;
- Licence of copyright in drawings to Employer – this is included in the standard form but is limited to the project for which the architect was engaged;
- That architect will give collateral warranties.

CR Engineers

Consulting Structural Engineer / Mechanical and Electrical Engineer

These are forms SE9101 and ME9101.

Some modifications that may be made to the standard form are as follows:

- Basis of Fees: both agreements contemplate that fees should be paid to the engineer either (i) as a percentage of the cost of the construction, (ii) on a lump sum basis, or (iii) on a time basis. It is up to the parties to agree the remuneration.
- Extensive provisions are set out in both documents giving rise to additional fees for various work items such as additional services, redesign of parts of a building, abandonment of works, and termination of the engagement. Where the employer seeks to negotiate a fixed fee with the professional it will be necessary to exclude these.
- PI Insurance obligation – Both forms oblige the engineer to maintain sufficient PI insurance to cover their liability under the engagement as long as it is available at commercially reasonable rates. The Employer might prefer to specify a particular level of insurance to be maintained for a particular period
- The forms do not deal with the giving of collateral warranties which may be requested by third parties with an interest in the project.

3 ANCILLARY AGREEMENTS – CR

3.1 Collateral Warranties

As you are no doubt aware, a collateral warranty in this context consists of a warranty in writing given by the professional to the employer and to other third parties. Why is this necessary? The answer is that collateral agreements may be necessary to protect the interests of third parties who are not



parties to the building contract but who have an interest in ensuring that the works are properly carried out. The purpose of a collateral warranty is to take the employer's entitlements under the building contract and extend that protection to third parties.

Typically the employer is the property developer who will enter into arrangements with third parties for the sale or lease of the property in question, possibly in a number of units, whether residential, commercial, or a mix of both. In the absence of a warranty directly from the professional, the beneficiary would have no comeback against the professional directly for loss arising from the negligence of the professional, say if there is a design flaw in the building. Beneficiaries of these warranties typically include the ultimate purchasers or lessees of the property, and the institution funding the development which will often have the right to take over the completion of the development in the event of default by the employer.

Typically a collateral warranty will deal with the same matters dealt with in the professional's appointment:

- Standard of care;
- Professional Indemnity insurance;
- Intellectual Property in drawings and specifications.

It is in the interest of the property developer to ensure that these warranties are sufficiently comprehensive.

An area of possible disagreement arises on the issue of the professional indemnity insurance. To ensure that the warranty will be acceptable to potential beneficiaries, the employer may request that the PI insurance be maintained at a particular level for a specified period.

This presents **two difficulties** from the professional's point of view.

- (i) Firstly, the professional cannot guarantee that its PI insurance will be available beyond the renewal date of its current policy.
- (ii) Secondly, there is a cost attached to the maintenance of the PI policy by the professional. The employer may take the view that the policy enures to the benefit of the professional's entire practice, and as such does not give rise to any additional cost beyond what the professional would have paid in any event. However, where the PI insurance requested by the employer is in excess of the cover which the professional has in place, this will give rise to an additional premium cost for the professional.

The standard letters of appointment provide that the professional should be obliged to maintain its PI insurance cover provided that this is available at commercially reasonable rates. This is somewhat unsatisfactory from an employer's point of view as there is no certainty as to what would happen if the insurance ceased to be available at those rates.

One arrangement that we have implemented in the past to deal with this is that the professional must notify the employer before allowing the policy to lapse, where rates increase beyond a specified point, to allow the employer to discharge the additional cost of the insurance directly.



3.2 Step-in Agreements – CR

In this type of agreement, which can sometimes be dealt with by a clause in the same document as the collateral warranty, the beneficiary is given the right to step into the shoes of the employer in order to engage the professional. Clearly from the point of view both of minimising disruption and possible delays, and for clarity on liability arising from the work of professionals, it would be undesirable for a beneficiary to lose the design team associated with a project where an employer has stepped out of the picture.

The step-in agreement is intended to allow the beneficiary to retain the services of the design team who may be obliged to notify the beneficiary before terminating their contracts of appointment, to allow the beneficiary to engage them directly to complete their work on the project.

Typically a step-in agreement will deal with the following:

- Professional consents to assignment of Employer's entitlements under building contract to beneficiary;
- Professional obliged to give notice to beneficiary of default by Employer under building contract;
- Beneficiary may assume obligations of employer directly or may nominate substitute;
- Beneficiary should undertake to pay all fees due at date of step-in and future fees.

CONCLUSION

The issues discussed above are but a sample of the issues relevant to design teams and each require careful scrutiny in advance of entering into any contractual relationship.

The above represents a brief outline of some of the legal issues and does not constitute legal or commercial advice. For further information on the subject, please contact Paul Keane at pkeane@rcmck.com.



