

**JUDICIAL INTERPRETATIONS OF THE TERM ‘LUMP SUM’
IN CONSTRUCTION CONTRACT**

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**A thesis submitted in partial fulfilment of the
requirements for the award of
Master of Science in Construction Contract Management**

**Faculty of Built Environment
University Technology Malaysia**

NOVEMBER 2009

ABSTRACT

Lump sum is a commonly used term in contract since the 18th century. Although the term is widely used in the construction industry, the interpretations and position of the lump sum contract in the eyes of the law is lacking which could contribute to dispute on rights and responsibilities of contracting parties. Failure of contract conditions to define the term interpretations could impact the overall project implementation and completion process. As such, the objective of this research is to investigate the judicial interpretation of the term lump sum in construction contract. In the legal textbook, the term lump sum is interpreted as fixed priced. It is also interpreted as a lump sum contract is one to complete the whole (sometimes termed as entire or a specific work) work for a lump sum. Based upon PAM Contract 2006 (with quantities), lump sum is fixed price and is not subject to remeasurement or recalculation except for provisional quantities and variations. The study had shown that none of the relevant cases had the judge himself given firm judicial interpretation of the term lump sum. Occasionally the term lump sum contract is referred to as entire contract. The doctrine that a lump sum contract has to be completed in practically all respects in order to qualify the contractor to get any money at all is very out of date. Lump sum itself is subject to adjustment because the court leans against a construction of the contract which would deprive the contractor of any payment at all simply because there are some defects or omissions. Whether a contract is an entire one is a matter of construction. Clear words are needed to bring an entire contract into existence. In the absence of such words, the ordinary lump sum contract cannot be an entire contract, for the courts to construe the promise to complete as a term and not a condition.

ABSTRAK

Istilah wang pukal biasa digunakan di dalam kontrak semenjak kurun ke-18 lagi. Walaupun istilah ini digunakan secara meluas di dalam industri pembinaan, kefahaman mengenai penafsiran dan kedudukan kontrak wang pukal dalam kehakiman undang-undang masih kurang yang mana ini boleh menyumbang kepada pertikaian mengenai hak dan tanggungjawab pihak yang berkontrak. Kegagalan syarat kontrak untuk menjelaskan penafsiran istilah ini mampu memberi impak dalam proses pelaksanaan dan penyiapan projek. Oleh itu, objektif kajian ini ialah untuk menyiasat tafsiran kehakiman ke atas istilah wang pukal di dalam kontrak pembinaan. Di dalam buku teks undang-undang, istilah wang pukal ditafsirkan sebagai harga tetap. Ia juga ditafsirkan sebagai kontrak wang pukal untuk menyiapkan semua (kadang kala diistilahkan sebagai seluruh atau tertentu) kerja untuk wang pukal. Berdasarkan Kontrak PAM 2006 (dengan kuantiti), wang pukal ialah harga tetap dan tidak bergantung kepada pengukuran atau pengiraan semula kecuali kuantiti sementara dan variasi. Kajian ini menunjukkan tiada kehakiman yang memberikan penafsiran sendiri yang kukuh untuk istilah ini. Sekali sekala istilah kontrak wang pukal dirujuk pada kontrak seluruh. Doktrin yang mengatakan kontrak wang pukal mesti disiapkan dalam semua hal secara praktikalnya bagi membolehkan kontraktor memperoleh sebarang bayaran adalah setinggalan zaman. Wang pukal itu sendiri cenderung pada pengubahsuaian kerana mahkamah enggan bersandar pada kontrak pembinaan yang mampu melucutkan hak kontraktor untuk sebarang bayaran hanya kerana terdapat sebarang kerja yang ditinggalkan atau kecacatan. Perkataan yang jelas diperlukan untuk mewujudkan kontrak seluruh. Dengan ketiadaan perkataan ini maka kontrak wang pukal biasa bukanlah kontrak seluruh yang membolehkan mahkamah menafsirkan yang janji untuk penyiapan adalah terma dan bukannya syarat.

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CHAPTER 1

INTRODUCTION

1.1 Introduction

This chapter will briefly discuss the background, objective, scope and the methodology of this research.

1.2 Background of Research

Lump Sum is the commonest form of construction contract¹ and the term is used in JKR 203B: Standard Form of Tender; *Having examined the Government's Requirement including instruction to Tenderers and the Conditions of Contract...we, the undersigned, offer to design, construct and complete the said Works in conformity with the said Pre-bid Documents for the **Lump Sum** of..... in accordance with the said Conditions of Contract*

Typically, the construction contract is placed through a tender exercise. This may be done by inviting tenders from a list of selected contractors, or through a general invitation. Each contractor submits a tender, sometimes accompanied by unsolicited offers on the base tender. The general expectation is that the contract

¹ Henry Henkin (1988). Drafting Engineering Contracts. England: Elsevier Applied Science Publishers Ltd. Page 120.

shall be awarded to the contractor who has tendered the most attractive price and terms in his bid. Alternatively, the client may decide on a particular contractor in advance and negotiate the price for the project with the owner pays the contract price in consideration for the contractor's obligation to construct and complete the project in accordance with the requirements as set out in the drawings, Bill of Quantities, specifications and other contract document.²

A contract is a legally binding agreement made between two or more parties, by which rights are acquired by one or more to acts or forbearances on the part of the other or others. These contractual agreements give rise to rights and obligations which the law recognizes and enforces.³ The purpose of Lump Sum projects is to reduce the costs of design and contract administration associated with quantity calculation, verification and measurement. This contracting technique requires the Contractor to submit a lump sum price to complete a project as opposed to bidding on individual pay items with quantities provided. The Contractor will be provided a set of bid documents (plans, specifications, etc.) and will develop a Lump Sum bid for all work specified in the contract drawings.

In a lump sum contract the contractor is paid a predetermined sum for completing a particular stage or the whole contract works. The sum is not adjusted to take into account any change in the extent of work from that estimated by the contractor at the time of contracting. The contractor therefore carries the risk of correctly estimating, at the time of contracting, the extent of work required to be carried out. The payment mechanism is easy to administer, provided the Owner does not vary the Works. If variations are likely contract terms will need to be incorporated to make provision for establishing an appropriate price on the basis either of a Schedule of Rates, or by negotiation or by reimbursement at cost. Inevitably variations on Lump Sum contracts give rise to many disputes and resolution of the Final Account may take some time.

² Chow Kok Fong (2004). Law and Practice of Construction Contracts. 3rd Edition. Singapore: Sweet & Maxwell Asia. Pg. 4

³³ David Barker & Colin Padfield (1992). Law. 8th Edition. Oxford, England: Butterworth-Heinemann Ltd. Page 112.

Lump sum is intensively used term in construction contract and there are many theories of lump sum available in law dictionaries and literatures. But what matters is the construction industry parties who are involved and applied this term of contract which has been used since the 18th century⁴. Lump sum contracts are the commonest form in building work and in mechanical and electrical engineering work and may be used in some civil engineering work where quantities of the various types of work cannot be fixed or accurately defined initially (at tender stage, where there is formal tendering).⁵

Although the term 'lump sum' is widely used in the industry, the understanding among contracting parties on the true interpretation of the term in construction contract is still lacking. Its subjective nature contributes to constant misinterpretation and the allocation of responsibility under a contract may not always be clear. As such, this research is to determine the judicial interpretation the term 'lump sum' in the construction contract. By understanding its true meaning, contracting parties can avoid unnecessary dispute with clearer understanding on risk and responsibility involved in accordance with the terms and condition of the contract.

1.3 Statement of Issue

In today construction contract, 'lump sum' is always the starting point where contractor is normally asked to fill bid of one sum for the cost of the whole tendered project. It is comparatively rare for the price the contractor is entitled to receive at the end of the day to be exactly the same as the lump sum. Lump sum to be paid to the contractor is unrelated to the actual cost to the contractor of completing the works. The lump sum is usually subject to adjustment for extra work, fluctuations

⁴ Christopher Hill (1999), Lump Sums: The Essentials. Retrived on 20th June, 2009, from www.building.co.uk

⁵ Henry Henkin (1988). Drafting Engineering Contracts. England: Elsevier Applied Science Publishers Ltd. Page 120.

sub-contractors, and so on. This has been the practice since there usually arise some inadequacy of the drawings or the contract specification. The position of lump sum in law is not widely understood.

Lump sum is a commonly used term in contract since the 18th century. Although the term Lump sum is widely used in the industry, the understanding among contracting parties on the interpretations and position of the lump sum contract in the eyes of the law is lacking which could contribute to dispute on rights and responsibilities of contracting parties. Its subjective nature contributes to constant misinterpretation and the allocation of responsibility under a contract may not always be clear. Failure of contract conditions to define the term interpretations could impact the overall project implementation and completion process.

All these issues have triggered author to conduct the research to identify issues brought to litigation pertaining to Lump sum or Lump sum contract. This is also to clear the misconception of the term in the agreement that supposed signifying that the parties are agreed together about the same thing. This research will give some overview on the issue on lump sum contract from the legal point of view. Hopefully, this research will give contracting parties better understandings of this commonly use terms. The outcome of the study may be used as lessons learned for Malaysia in pursuing all its lump sum projects.

1.4 Objective of Research

The objective of this research is to determine the judicial interpretation of the term Lump sum in construction contract.

1.5 Scope of Research

The approach adopted in this research is case law based way by literatures from selected legal textbook will be used in search of the interpretation. Selected standard forms of contract will also be referred to and they are as follows:

- (i) PWD 75 (Rev. 12/06): JKR Sarawak Standard Form of Contract;
- (ii) PWD Form 203A (Rev. 2007): JKR Standard Form of Contract;
- (iii) PAM Contract 2006 (With Quantities): Agreement and Conditions.

Related law from Contracts Act 1950 (Act 136) will also be used in this research. Due to time constraint, all related case laws in relation with the subjective nature of the legal interpretation were searched via *Lexis Nexis* website⁶ through its own search engine and limited to cases reported in Malaysia, Singapore and Brunei as at 31st July, 2009. The keywords used in the search were -lump sum and construction contract.

1.6 Significance of Research

This research will investigate the subjective nature of contract interpretation of the term -lump sum from the judge interpretation based on the findings of the case. In addition, the research will also report the interpretations from available legal textbooks and finally the judicial positions when dealings with lump sum contract.

This research will present findings of the investigation from selected cases which will show evidence that contracting parties interpret the contract differently. The intention of this study is to bring forward the actual interpretation of -lump sum. By knowing this commonly used contract's true effect, this will assist contracting players to have better understanding on obligation under this contract. This will be a

⁶ <http://www.lexisnexis.com>.

measure to manage potential risk, thus appreciation of the lump sum's true interpretation will enable better decision making.

1.7 Research Methodology

This research involved literature review on the legal term lump sum in the construction industry. Initial study will be carried out involving extensive reading and understanding of the theories involved from legal textbook.

Then data and information collecting will be carried out. Primary source will be law cases found in Malayan Law Journal through the access of *Lexis Nexis* available in the university's online database. Secondary sources such as articles, journals, textbooks and related websites will also be studied and referred to in the course of the whole research.

Analysis will be done on collected information and will be arranged in an orderly manner and writing up will be carried out, followed by checking and correction of writing.

1.8 Research Structure

This research consists of five chapters. The brief descriptions of each chapter are as follows:

Chapter 1: Introduction

This chapter presents the overall content on the study and a brief report on the processes involved in carrying out this research. It introduces the background of the study, relevant issue, objective and method to achieve the objective.

Chapter 2: The Construction Contract

This chapter concentrates on discussing placement of contract, various type of contractual arrangements, the features in construction contract and the contract document that uses the term 'lump sum' as part of the formation of the contract document. The theories and rule of interpretation of in order to understand the meaning of the term 'lump sum' in construction contract will also be discussed in detail. This involved literature review from books, journals and other reliable sources to provide true understanding of this contract.

Chapter 3: 'Lump Sum' in Construction Contract

This chapter discussed on theories and issues in relation to the law of lump sum. Topics related to 'lump sum' in construction contract from various literatures will be listed and reported to assist understanding of the subject matter. The terms normally found in construction document contract in relation with 'lump sum' from relevant sources of information will be archived and analyzed and all findings from this exercise will be identified and presented in organized manner.

Chapter 4: Judicial Interpretations of the Term ‘Lump Sum’ In Construction Contract

This chapter analyzed selected cases in relation with this research from the judicial decisions as reported in law reports which are related to the research issue on ÷lump sumø. All cases are discussed in detail, analyzed and present in scheduled form. Besides that, positions of court when dealing with ÷lump sumø contract will also be reported with in depth discussion of the relevant issues.

Chapter 5: Conclusion

This chapter will compare all findings on the relevant ÷lump sumø theories and judicial interpretations and judgments from previous chapters. This chapter will also bring forward findings on judicial positions when dealings with ÷lump sumø contract. After that, the constraint found during this research will be reported.

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