

RISKS IN THE PAM 2006 STANDARD FORM OF CONTRACTS

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RISKS IN THE PAM 2006 STANDARD FORM OF CONTRACTS

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To my beloved father, mother and sisters.

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Thank to God I was able to complete this master project perfectly without any complications.

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ABSTRAK

Industri pembinaan adalah antara salah satu industri yang dinamik, mencabar, memuaskan dan juga berisiko. Ia melibatkan banyak ketidakpastian dan kebarangkalian yang membuatnya terdedah kepada risiko. Amnya risiko boleh dikatakan peristiwa atau keadaan yang tidak menentu di mana kejadiannya boleh menjejaskan objektif projek serta meninggalkan kesan yang negatif. Borang kontrak standard yang digunakan untuk mengikat hubungan yang boleh dikuatkuasakan oleh undang-undang antara pihak-pihak yang berkontrak juga boleh menimbulkan beberapa risiko. Objektif kajian ini adalah untuk mengenal pasti risiko yang terdapat dalam Borang Kontrak PAM 2006 dan menegenal pasti kemungkinan berlaku serta tahap kesan risiko yang dikenal pasti dalam objektif pertama. Kajian ini telah dijalankan dengan menggunakan peringkat dalam proses pengurusan risiko. Pertama sekali risiko-risiko dalam terma dan syarat kontrak dikenal pasti dengan menggunakan teknik kajian dokumentasi. Kemudian, risiko-risiko tersebut telah dikelaskan kemungkinan berlakunya risiko dan tahap kesan risiko menggunakan kaedah kajian soal selidik. Hasil kajian menunjukkan bahawa terdapat 46 risiko daripada 23 klausa berbeza yang telah dikenal pasti dalam terma dan syarat Borang Kontrak PAM 2006. Di antara risiko-risiko tersebut, untuk penilaian kebarangkalian, 10 risiko didapati hampir pasti berlaku diikuti dengan 31 risiko pasti mungkin berlaku dan 5 mungkin berlaku. Sementara itu, bagi penilaian kesan, 27 risiko akan meninggalkan impak yang sangat tinggi kepada objektif, diikuti oleh 19 risiko kesan tinggi. Kesimpulannya, risiko wujud dalam terma dan syarat dalam kontrak dan ia harus difahami sebelum perjanjian kontrak ditandatangani untuk elakan salah faham.

ABSTRACT

Construction industry is among one of the dynamic, challenging, satisfying and also risky industries. It involves around many uncertainties and probabilities which is indirectly exposed to risk. Generally risk is known as an uncertain event or condition in which its occurrence could affect the project objective and most likely to leave a negative impact. These risks in construction are said to be present from the earlier stage of project such as feasibility stage till the completion stage. The standard form of contract which is used to bind a legal relationship that is enforceable by law between the contracting parties also has some risk. The objective of this study is to identify the risk found in PAM Contract 2006 and to identify the risks probability of occurrence and level of impact. This study had been carried out by using the stages in risk management process. Firstly the risks in terms and condition of contract are identified using the documentation review technique. Later, those risks were ranked according to the probability of occurrence and the level of impact of each risk by conducting a questionnaire survey. The result indicates that there were 46 risks from 23 different clauses identified in terms and condition of PAM Contract 2006. For the probability ranking, there are 10 risks which are almost certainly to occur followed by 31 risks certainly to occur and 5 risks that are likely to occur. Meanwhile for the impact assessment, 27 risks would be leaving very high impact to the objective followed by 19 high impact risks. Overall it can be concluded that risk do exist in terms and condition and one should really understand those terms before entering into contract to avoid any risky events that could affect the project.

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LIST OF ABBREVIATIONS

PMBOK	-	Project Management Book of Knowledge
PAM	-	Persatuan Arkitek Malaysia
PWD		Public Work Department
JKR		Jabatan Kerja Raya
CIDB		Construction Industry Development Board
IEM		Institution Of Engineers Malaysia

CHAPTER 1

INTRODUCTION

1.1 Background of the Research

Construction is the process of combining materials, machinery, people, technology and the environment to produce construction products such as buildings, bridges, roads and highways etc. by applying specific knowledge and know-how. It involves many separate teams, firms, companies and hundreds of interrelated activities, tasks and work packages which are organized in logical and systematic manner.

The process starts with one wants to build a building, followed by design, documentation, tendering, contracting, construction and completion. Outline of the project procurement process from inception to completion, the process of selection of contractors and the execution of contract and contract documentation. Construction contract document is a document which consists of several other documents inclusive of the standard form of contract.

Usually the contract between the employer and contractor is sealed using the standard form of building contract. Standard form of contract contains the terms and

condition of the contract which are more likely to highlight the obligation of employer and contractor in the contract. Today, there are various standard form of contract used in construction industry including PAM, PWD, CIDB and IEM form of contracts. As the matter of this research, it would be involving around PAM Contract 2006 and the terms and condition together with its allocation of obligation and liability between employer and contractor.

Despite of the type of project, generally construction industry is a dynamic, challenging, satisfying and also risky. It involves many uncertainties and also exposed to risk because of the activities of the construction business, natural processes and also the organization.¹ The terms and conditions laid down in the PAM form of contract spells out the rights, obligations, liabilities of the contracting parties and the probable implication on them. These terms and conditions may contain risk to both the employer and contractor.

In order to understand that obligations, both the parties must first thoroughly understand the risk distribution or probability that are pose by the respective standard form of contract that are used. Not only the contractor have to realize and understand his obligation to complete the project with minimum risk, but the employer also must know and understand his obligation toward contractor in minimizing the construction project risk.

1.2 Statement of Problem

The foregoing discussion highlighted some pertinent issues associated with the use of the PAM Standard Form of Building Contract 2006. Firstly, do the

¹ Salihudin Hassim, M. S. (2009). The Contractors' Perception Towards IBS Risk in Construction Projects in Malaysia. *The Professional Journal of The Surveyors Malaysia, Volume 44*, 14-19

parties, both the employer and contractor have a clear idea of the type, nature or magnitude of the risk that they will probably have to take upon themselves? Secondly, what exactly are the type, nature and magnitude of the risks that can be found in the clauses of PAM Contract 2006? Thirdly, how often do the risks laid in the clauses would occur in a real project? Fourthly, how do we minimize the impact of the risks?

These issues are the inherent risks built into the terms and conditions of contract which must be accepted by the contracting parties (employer and contractor) when they enter into the contract. Subsequently, those questions later turned out to be the main issues which had been used to perform and form this research.

1.3 Research Question

The statement of problem highlighted earlier is the main essence of the research. However, to address all the issues in this research might not be feasible because of the time limitation. So those issues had been simplified and two main questions were formed. The two research questions are:-

1. What are the risks that can be found in the terms and condition of PAM Contract 2006?
2. What are the probability of occurrence and level of impact of the risks?

1.4 Aims and Objectives of the Research

There are two objectives formed for the research out from the research question, which are:-

1. To identify the risks in the terms and conditions of PAM Contract 2006.
2. To identify the probability of occurrence and level of impact of the risks.

1.5 Scope of the Research

Earlier, there has been research done which is quite similar to the theme of this research. However, there are major differences between this and the previous research. The previous research done was about the risks pose by the terms of contract in JKR standard form of contract. The identification also was only focused on several selected clauses by the researcher. However as for this current research, it will mainly focus on PAM Contract 2006 standard form of building contract. In addition, all the clauses in the form will be used to identify the risks carried by its terms and condition.

Throughout the study, the PAM Contract 2006 form are mainly referred for identification process together with some documents, papers and books linked to the identification process. Even though it is mainly a documentation research, some pilot studies and surveys are done by distributing questionnaire to help and validated the documentation of characteristic.

1.6 Significant of the Research

This research is significant to be conducted as by conducting this research, the details and essence of the clauses could be looked into. The clauses of the form and the risks contain in it would be understood clearly by the contracting parties. Understanding the clauses risks could help the contracting parties fully aware of their role and obligations while avoiding any major disputes. The knowledge on the clauses also could help the parties to handle and resolve any disputes that may arise.

1.7 Research Methodology

In every research that will be conducted, research methodology would be surely constructed to determine organized steps to conduct the research. Each methodology which is designed for a research should be carefully designed for it to suit the research. It is important as correctly organized steps are important to make sure that a research is carried out smoothly without any problem and reaches its objective.

In this research, there are five main stages which are designed to carry out the research. Those stages are as follows:-

- (i) First Stage (Development of Proposal),
- (ii) Second Stage (Research Design),
- (iii) Third Stage (Data Collection),
- (iv) Fourth Stage (Data Analysis), and
- (v) Fifth Stage (Conclusion and Recommendation)

All those stages will be elaborated more in the following subtopics below.

1.7.1 First Stage (Development of Proposal)

In the earlier stage of research, discussion with supervisor held to get some fresh ideas on topics that could be researched. The problem and purpose of the research were also obtained. Therefore in this stage; the topic, issues and problems of the research were determined and an objective and scope of research were formed.

1.7.2 Second Stage (Research Design)

This stage involved the process to determine the types of data needed to be collected for the purpose of research. The collected data are divided into two, which are the secondary data and primer data. Secondary data is the data which is known as the literature review of the research while primary data is the data that are collected via the research.

1.7.3 Third Stage (Data Collection)

This stage involved the secondary and primary data collection which is related to the research. As per mentioned above, the secondary data collected via reading materials that are related. Whereas for the primary data, it was collected using the documentation analysis method.

1.7.4 Fourth Stage (Data Analysis)

This is the stage where the collected data were analysed. A suitable analysis method was chosen for the collected data.

1.7.5 Fifth Stage (Conclusion and Recommendations)

This is the last stage in a research which involved the conclusion making to thoroughly answer the research objective using all the data that have been collected.

1.8 Chapter Organization

Below are the brief contents of each chapter contained in this research. This research contains 7 chapters as follows;

i) Chapter 1 : Introduction

The first chapter of this research is the introduction of research which comprises the background of study, problem statements, research questions, aims and objective, scope of the research, significance of the research, research methodology and also the chapter organisation.

ii) Chapter 2 : Construction Project Procurement and Contract

This is a chapter of literature review in which some the related reading material were referred to. The topics contained in this chapter are introduction, construction project procurement, construction contract, the terms and conditions of construction contract and contract documents and the standard form of contracts.

iii) **Chapter 3 : Standard Form of Contract**

This is also a chapter of literature review in which it contains the review of standard form of contract. This chapter comprises the topics of introduction, PAM standard form of contract and types, the content of the PAM Contract 2006, outline of the terms and conditions of the contract and also the conclusion of chapter.

iv) **Chapter 4 : Risk**

This is also a chapter on literature review which focuses on risk. This chapter contains chapter introduction, definition and classifications of risks, risks in construction, risks management and also chapter conclusion.

v) **Chapter 5 : Research Methodology**

This chapter comprises on the methodologies that were used to conduct this research. The subtopics under this chapter are development of research proposal, research design, data collection, data analysis and conclusion and recommendation.

vi) **Chapter 6 : Risks in the PAM Standard Form of Building Contract**

This chapter focuses on analyzing the collected data and discussing the findings from the analysis. The analysis and discussing were done with regard to achieve the research aim and objective.

vii) Chapter 7 : Conclusion and Recommendation

This chapter is about the final conclusion and summary of the research. It also contains some recommendations regarding the study and also for further researches.

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