

UNDERSTANDING CONTRACT DOCUMENTATION

Mohamad Ibrahim Mohamad¹ and Zulkifli Madon²

¹CTMC, Fac.of Civil Eng., UTM, 81310 Johor Bahru, Malaysia.

E-mail: drm2i@yahoo.com

² Director, Public Work Department, Negeri Sembilan, Malaysia.

ABSTRACT : The contractual obligation by any party in any contract will be interpreted by terms and contents of the documents laid down in the contract. Effective interpretation and understanding of the contractual obligations will be much dependent on the clarity of the documents in translating the needs and requirements implied as in the agreement. Without proper understanding of the documents may lead to the different interpretations which may result in unnecessary contractual problems such as disputes, unnecessary claims, reworks, shoddy works, and even litigation. This paper presents the results of the study related to issue of understanding of contract documentation done in Malaysia. The findings presented include the factors that inhibit the understanding of the contract as well as the factors that can help to make the interpretation process much easier. The paper also suggested various factors that can be used to improve the level of understanding of contract document that can be considered in designing the contract document.

Keywords: construction contracts, understanding contract documentation, factors that support and inhibit contract understanding , improving contract document.

1. INTRODUCTION

Contractual obligation by any party in any contract will be of questionable state if the understanding of the terms and interpretation of the contents of the contract documents are not fully appreciated. The contract documents drafted for any contract should fulfill the intended roles of being the references and guidelines for the relationships between the contracting parties throughout the project. Factors of contractual language and its judicial interpretation may lead to the problem of understanding of the needs of the contract which may lead to misinterpretation and misunderstanding of the facts in contract obligations. This situation may prevail an opportunistic party to take the unfair advantage of another party when an adjustment to be made in the contract. Therefore it is necessary to have proper understanding of the contents of the contract documents which leads to the enhancement of the contractual relation and assurance of the intended deliverance of the product.

The complexity of contract documentation in a construction contract most of the times hinders the contract participants especially the contractor and the clients to really understand the contractual needs and obligations of the parties. The various backgrounds of the contractors in our construction industry especially in the public sector in Malaysia contribute to difficulties in delivering the required product to the clients. Therefore, understanding the contents and requirements of the contract documents will have great influence in the smooth and good performance of the construction project.

2. Understanding the Contract Requirements

The constructions contracts express the intent of parties and memorialise their principal risk allocation decisions (McCallum, 2002). To understand the contract requirements is to understand the contents of the documents and the spirit of the contractual relationships. Contracts are formed and signed based on the fair basis where parties agree amicably to discharge their obligations to satisfy each other needs and requirements.

Indeed as construction are a complex and challenging process it requires interpretation of conformance with myriad laws, code and regulations, marshalling of considerable resources including labor, equipments, materials and good communication and coordination among multiple parties involved in the project. Many factors are unknown or unknowable at the start of any project. This detail understanding of the whole requirements and process of the contract are essential in order to minimise the construction risks that may lead to unnecessary problems such as disputes, claims, litigation, shoddy works, and reworks even lost of future business relations. The effects of construction disputes are detrimental. If disputes are not properly managed, they may cause project delays, undermine team spirit, increase project costs, and, above all, damage continuing business relationships (Chan and Suen, 2005).

The proper allocation of responsibilities is a crucial factor in determining whether a particular construction contract should be considered 'a good' contract. McCallum (2002) characterised a good contract clearly informed such party what it must do and to what it is entitled. It also informs each party of their right if the other party does not performed as pronounced. It anticipates the likely problems and resolved them clearly and in away strikes the parties as a proper allocation of risks and responsibilities. A good construction contract of course, includes well drafted drawings and specifications that inform the contractors what he must do to earn the promise compensation and provide a method of determining whether the objective has been reached.

3. Methodology of the study

The first stage of this study includes the appointment of fifteen panel's member of experts that have vast experience in construction contract related aspects. These included lawyers, professionals like senior engineers, quantity surveyors and project managers. The data were collected using face to face interviews and structured and open-ended questionnaire form given for these experts to respond. In many cases more than one meeting were arranged with them. The panel of experts has been queried on the issue related to the importance of understanding of contract documentations, the expected level of understanding of contract documentation as well as factors that support and inhibit its understanding. This was followed by the distribution of the industry wide questionnaire survey to the sixty five respondents which represent the contractors involved in public sector projects in Malaysia. A total of 94% of the respondents returned the questionnaires and completely answered all questions given. The questionnaire investigated most of the issues as being presented to the panel of experts but in more comprehensive and structured manner. As a strategy to simplified the process of generating the responses in the form of qualitative data from the industry wide questionnaire survey, a Likert Scale of an ordinal scale of 1 to 5 in ascending order of agreement had been in most of the questions or statements given for the respondents to rate their opinions. The result of the responses presented in this paper is calculated using Relative Index method which represents the strength of response from 0.2 to 1.0 for each statement where 1.0 indicate 100% strongly agreed by all respondents and 0.2 is 100% least agreeable. This technique using RI has been used by Nesan (1997) and Holt et al. (1996) in the same context of application.

4. Expected Level of Understanding of Contract Document

The questions related to the level of understanding are only presented to the panel of experts. In the content analysis of the interviews result it is found that all the fifteen respondents agreed that contractor has to be well verse in interpretation of the conditions and requirements of the contract. All of the panel members also agreed that contractors in Malaysian construction industry do not bother to understand the contract documentation until when problem persist. The level of understanding toward contract document by the contractors is

still at medium level and if they were given a rating of scale zero to ten, they will qualify between five and six. This indicates that much effort has to be done in order to improve the understanding toward contract document for these contractors. The panels also feel that contractors need to have the right attitudes in order to excel in the understanding of contract documents.

5. Importance of Understanding of Contract Documents

The study has determined that the understanding of contract documents is very important in order to achieve effective outputs in contract implementations. The content analysis from the interview with the expert panel has shown that lacking in understanding of contract documents will lead to serious contractual problems and the output of the projects will be affected in term of quality, cost and time. The panels also agreed that the level of understanding of contract document has to be improved for best output of the contract practice with regard to cost, quality and time. These findings were further reinforced with the outcomes of the industry wide questionnaire survey as indicated in table 1 as follows.

Table 1: The Importance of Understanding of Contract Documentation

Question	Relative index
For effective Implementation of a project the contractor must have the ability to understand the contract document thoroughly	0.95
Understanding of contract document is very relevant and important in order to sustain the desired cost, time and quality in project implementation.	0.91
Failure to understand the contract document will lead to serious contractual problems and disputes	0.90
Failure to understand the contract document may lead in unnecessary argument between parties and result in lost of reputation and business.	0.87
Failure to understand the contract document will lead in misinterpretation of the needs of the contract which result in lost of trust among the contracting parties.	0.85
Failure to understand the contract document potentially leads to mistakes in implementation of project which caused unnecessary rework and increase in project cost.	0.84

As summary findings from the industry wide survey the study have revealed that the contractors themselves agreed that the ability to understand the contract documents is critical in order to achieve the effective implementation of the project. Problems such as disputes, cost overrun, and bad quality are also the results of lacking in understanding of the contract documents. Ignorance in the ability to understanding the contract documents are potentially the caused of most contractual problems since these ability will depend very much on the knowledge, exposure and the experience of the contractor over the subject.

6. Factors that Influence the Understanding of Contract Document

Based on the analysis done on the structured questionnaires given to the panel of experts they have strongly agreed that the understanding of contract document are very much influence by the factors of attitude This is shown by relatively high scores in relative indices of the factors where Attitude scores RI 0.89, followed by Education Background score RI 0.87, Past Experience scores RI 0.85 and Commitments scores RI 0.85. These factors have also been

agreed by the respondents in the industry wide survey as shown in *table 2* where the value of relative indices are very high showing that they are very relevant in contributing to the subject. The experts have the opinions that among all the four factors attitudes prevail in the top rank followed by education background, past experience and commitments. This is in contrary when dealing with the opinions of the contractors in the industry who feel that past experience will have the priority followed by competency, attitude and education background, education background, past experience and commitment. The argument are, being the experts of quite different backgrounds and with relatively highly educated and experience in their field they may thought that one to have the right attitude in order to succeed in their undertaking followed by the education background or knowledge in the subject.

Table2 Factors Influence the Understanding of Contract Documents

Question	Relative Index (RI)
Past Experience	0.91
Competency	0.90
Attitude	0.87
Education Background	0.86
The complexity of contract documents always hinders the contractual parties to understand the actual need of the contract	0.84
Different class of contractor has deferent level of understanding toward contract documentations.	0.80

Having instilled these as their priority then experience will have of benefit to ease the undertaking together with the commitment in their selfness in striving for future excellence. It is noted that the contractors in the industry believed that experience and competency are the first two most important followed by the attitude and education background. The findings has shown slightly different in priority in ranking the factors but the analysis shows that contractors are having experience of two to more than twenty years experience and 61% are having experience of 11 to more than 20 years. In this situation they may felt that experience will prevail in all respect in order to master the understanding of contract documents. Anyway in both cases the study has shown that all factors have relatively high scores which indicate that both respondents in the expert and in the industry has the same trend of opinions that all the factors has strongly contribute to the understanding of contract documents.

Based on the content analysis of the open ended questions given to the experts there are several additional factors given by the expert panel that they believed to influence the understanding of contract document. These factors have been suggested based on the experts experience in their undertaking pertaining to the subject matter. Those factors are: the used of simple language; adequate knowledge; clarity in document; and regular training.

7. Factors that Inhibit Understanding of Contract Documentation

The study continues with the determination of the factors that inhibit the understanding of the contract documentation. The result of the analysis of the interviews with the expert panel has established the following factors that can inhibit the understanding of the contract document. Those factors are: contractors experience ; competencies; negative attitude toward effort to understand; lack of good education background; and complexity of contract document itself.

Based on the analysis on the questionnaire in the industry wide questionnaire survey, the main factors that inhibit the understanding of contract documentation are presented in the *table 3*.

It is noted that complexity of contract documents will also influence the contracting party to understand the contract documents. This is particularly true when contract documents have a lot of legal jargons and phrases sometimes may have irrelevant materials associated to it. This will result parties in the contract may have difficulty to understand the terms used in the contract. Document that having irrelevant materials may lead to misinterpretation of the actual need of the contract and will hinder the contractor to understand the contract. In relation to this, these complexity of the documents are due to many reasons such as the use of difficult languages, specifications used are not clear and illogical in nature, clients do not clear the requirements needed and no familiarization with the types and form of contract used. These elements will create confusion to most parties in the contract and will lead to not relevant materials may be included in the documents which increase the thickness of the documents.

Table 3 Factors Inhibit Understanding of Contract Document

Question	Relative Index (RI)
Documents are too thick and too many legal phrases.	0.81
Client do not aware of their requirements	0.76
Never having any training	0.75
Fully delegate to subordinates	0.74
Requirements are not clear and too general	0.74
Language used is difficult to understand.	0.73
Time consuming in understanding the contract.	0.69
Specifications are too stringent and not practical.	0.68
Not familiar with the contract forms used	0.68
Seldom read the documents.	0.68
Never had any experience with the same project	0.66

There are cases where the understanding of the documents will be affected when these contractors are deficient in qualified personnel in their organization. As shown by the experts that the contractors in our local industry may have problem in inculcating the habit of reading the contract documents which further hinders the contract participant border to understand the contract documents. When referring to the basic resources, it is true that small contractors will have small strength in term of resources such as qualified personnel and capitals. This will affect the level of the understanding when training needs for the personnel does not in the priority agenda of the organization.

8. Improving the Understanding of Contract Document

The panel of experts through one of the open ended question used in this study has expressed their views of how to ensure better understanding toward contract documents by the contractors. Among the most frequently quoted factors as proposed by the expert panel to improve the contract understanding are: regular training for contractors; engagement of qualified personnel; clarity in the contract document itself; and the used of simple language. It is noted that some of these factors have been proposed in the structured questionnaires for the panel in this study but nonetheless they were proposed again in the open ended question showing that their most importance in contributing to the issues. The same issue has been explored in the industry wide questionnaire survey and the findings are tabulated in *table 4*.

As mentioned in the previous discussion contract documents are sometimes complex and contained legal phrases and they are prepared by the qualified personnel thus interpreting the documents likewise need the qualified personnel too. In this situation the contractors has to be prepared so as to have equivalent qualifications in order to satisfy the situation. Therefore regular training program is one of the activities as the effective way to improve the level of

understanding towards contract documents. These training need programs are also proposed by the contractors as the respondents in the industry where they have been strongly agreed that in all cases the contractors has to be well trained and they should attend the mandatory induction course before they have to start in any contract activity.

The responsible agency that govern the contractors is proposed by the respondents to rank the contractors based on their qualifications and training backgrounds and they even strongly agreed that test on qualification assessment has to be carried out in order to sustain their qualified status. In this respect it is proposed to be the responsibility of the agency to initiate proper guidelines for registration of the contractors with respect to the qualifications, training needs for developing skills and competencies, and controlling the requirements for qualified registered contractors.

The clarity of the contract documents is considered another important factor to improve the understanding of contract documents. Clarity means easy to understand and parties have no difficulty in translating the documents. All respondents strongly agreed that this factor have to be considered when preparing the contract documents. Clarity is also related to using the simple language and includes many other things as shown in *table 4*.

Table 4: Factors in improving understanding of contract document

Factors that can help to improve understanding of contract document	Relative Index(RI)
Sincerity in contracting	0.95
Drawing must be clear and checked by all parties.	0.95
Clarity in contract document for better understanding toward contract documents.	0.93
Client's requirements must be clearly understood.	0.92
Contract document should be written in simple language.	0.91
Establish good communication relationship.	0.91
Contract document must be precise, objective and practical	0.90
Qualified personnel to prepare the contract document.	0.90
Regulatory requirement to be clearly explained.	0.89
Bill of Quantities to be clearly and objectively detailed.	0.89
Minimise use of complicated legal phrases.	0.88
Provide well trained personnel for every project to interface the contract.	0.87
General condition of the contract to be made familiar	0.86
Construction work specifications to be simple and suit class of contractor.	0.81
Mandatory induction session for a contractor before any contract to be implemented	0.76

Despite much have been said about factors to improve the understanding of contract documents, the respondents in the industry also agreed that sincerity is also contributing in improving the understanding of contract documents. This factor is also closely related to other personal factors such as attitudes, commitments, and the personal will force to master the subject. The respondents have been also suggesting the two ways communication discussion session to be held in aid to the needy contractors in every award of the contract before commencement of the works. The suggestions may be included in the training program or can

also be address by the governing agency when giving assistance in litigation aid for the needy contractors as suggested by the respondents.

10. Conclusion

This paper has highlighted a critical issue related to the understanding of the contract document to ensure successful delivery of the construction project. Various factors that support and impede the understanding of the contract documentation have been determined. Also presented are the factors that can help to improve the understanding of the contract documents.

11. REFERENCES

- Chan, E. H. and Suen, C. H. (2005). Dispute and Dispute Resolution System in Sino-Foreign joint Venture Construction Project in China. *Journal of Professional issues of Engineering Education and Practice*. ASCE / April 2005/141
- Mc. Callum, M.H.(2002). A Quick Primer on Construction Risks And Contracting Practice. *American Corporate Counsel Association Annual General Meeting*. October 2-4, 2002.
- Holt, G.D., Olomoaiye, P.O., and Harris, F.C. (1996) *Tendering Procedures, Contractual Arrangements and Latham: The Contractors' View*. Engineering, Construction and Architectural Management. pp 97-15
- Nesan, L.J. (1997) *A generic model for effective implementation of empowerment in Construction contractor organisation*. Ph.D. thesis, University of Wolverhampton.