

RESERVATION OF RIGHTS IN CONSTRUCTION CLAIMS

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DEDICATION

To my beloved father Larry,
my mother Ceciline,
my siblings Larry Jr and Larisa,
to Ayen and Jesus.

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ABSTRACT

One of the common problems faced by contractors and project owners is their entitlement to claim for extension of time for delays and/or damages. It is understandable that not all projects have contract managers to advise the parties on every step of claiming procedures. Hence in most cases claimants are barred from asserting their claim due to failure of giving notices to claim or reserving their rights to claim. Most construction contracts require the notices as a condition precedent for claim entitlement. Contractors and project owners turn to reservation of rights (ROR) statement as a form of prompting the other party of their intention to claim in future, most of the time, for the unforeseeable and unknowable causes (ie. direct and indirect impacts of loss and/or expense, impacts of delays, additional compensation for numerous variation orders, damages due to defective works by contractor after the conclusion of final account, and other claims that cannot be assessed in the moment of issuing the notices). Alternatively, it is quite common for contractors and project owners to turn to ROR statement as a form of prompting the other party of their intention to put forward their claims in the future. The validity of the practice of ROR has been subject to dispute and there seem to be some conflicting judicial interpretations from the bench. It has been held that the ROR disregarded the condition precedent requirement. The purpose of the research is to determine the principles that judges used in upholding or denying the use of ROR statements in the construction claims. There were six (6) cases relevant to ROR in construction claims that were analysed in this research, three (3) were from the Malaysian jurisdiction, two (2) from the American jurisdiction and one (1) from UK jurisdiction. It is found that principal reason for denying the ROR was the failure of the claimant to conform to conditions of a proper notice when using the ROR; while the fundamental reason for upholding the ROR is because notice is not a condition precedent and the claim could not be established pursuant to any clause in the construction contract. It remains that an ROR will only stand provided that the notice is not a condition precedent to a claim.

ABSTRAK

Salah satu masalah biasa yang dihadapi oleh kontraktor dan pemilik projek adalah hak mereka untuk menuntut lanjutan masa atau lanjutan masa dan/atau ganti-rugi. Adalah difahami bahawa tidak semua projek mempunyai pengurus kontrak yang memberi nasihat kepada pihak-pihak tentang prosedur membuat tuntutan. Oleh itu, dalam kebanyakan kes, pihak menuntut gagal mendapat tuntutan mereka kerana kegagalan memberi notis untuk menuntut atau menyimpan hak mereka untuk menuntut. Kebanyakan kontrak pembinaan memerlukan notis sebagai syarat terdahulu untuk tuntutan hak. Para kontraktor dan pemilik projek menggunakan mekanisma 'menyimpan hak' (ROR) sebagai satu mempertahankan hak mereka untuk menuntut pada masa akan datang, pada masa yang sama, untuk sebab-sebab yang tidak dapat dijangka dan tidak dapat diketahui (iaitu kesan langsung dan tidak langsung dari kerugian dan/atau perbelanjaan, kesan penangguhan, pampasan tambahan untuk pelbagai pesanan variasi, ganti rugi akibat kerja yang salah oleh kontraktor selepas penutupan akhir akaun, dan tuntutan lain yang tidak dapat dinilai pada saat mengeluarkan notis). Sebagai alternatif, ia adalah perkara biasa bagi kontraktor dan pemilik projek untuk beralih kepada kenyataan ROR sebagai satu bentuk yang mendorong pihak lain niat mereka untuk mengemukakan tuntutan mereka pada masa akan datang. Kesahihan amalan ROR telah menimbulkan perselisihan dan nampaknya ada beberapa tafsiran kehakiman yang bertentangan dari mahkamah. Ada hakim yang memutuskan bahawa ROR bertentangan dengan pematuhan syarat terdahulu. Tujuan penyelidikan adalah untuk menentukan prinsip yang hakim gunakan dalam menegakkan atau menafikan penggunaan pernyataan ROR dalam tuntutan pembinaan. Terdapat enam (6) kes yang berkaitan dengan ROR dalam tuntutan pembinaan yang dianalisis dalam kajian ini, tiga (3) dari bidang kuasa Malaysia, dua (2) dari bidang kuasa Amerika Syarikat dan satu (1) dari bidang kuasa United Kingdom. Adalah didapati alasan utama untuk menafikan ROR adalah kegagalan pihak menuntut untuk mematuhi syarat-syarat notis yang sewajarnya apabila menggunakan ROR; Sementara alasan asas untuk menegakkan ROR adalah kerana notis itu bukan merupakan syarat terdahulu dan tuntutan itu tidak dapat mematuhi mana-mana fasal dalam kontrak pembinaan. Sebagai rumusan ROR hanya akan terpakai dengan jika tidak terdapat syarat notis terdahulu atau ROR itu memenuhi syarat terdahulu untuk tuntutan..

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LIST OF ABBREVIATIONS

AI	Architect's Instruction
AIA	American Institute of Architect
BLR	Building Law Reports (UK)
CAI	Confirmation of Architect's Instruction
CO	Change Order
EHWC	High Court of England and Wales
EI	Engineer's Instruction
EOT	Extension of Time
EWCA Civ	Court of Appeal of England and Wales (Civil Division)
JCT	Joint Contracts Tribunal
LAD	Liquidated and Ascertained Damages
MLJ	Malayan Law Journal
MLJU	Malayan Law Journal Unreported
NTC	Notice to Claim
PAM	Pertubuhan Akitek Malaysia
PWD	Public Works Department
ROR	Reservation of Rights
SGHC	Singapore High Court
SO	Superintending Officer
UKPC	United Kingdom Privy Council
UKHL	House of Lords, United Kingdom
VO	Variation Order

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CHAPTER 1

INTRODUCTION

1.1 Background of the Study

The primary purpose of the construction contracts is to bind the parties and to enforce the rights and responsibilities of the parties in order to complete a project. Within the project's life cycle, claims commonly arise between the parties to the construction contract. Claims are made for additional payment of variation works¹, extension of time², direct loss and/or expense³, liquidated damages⁴ (LAD) and so on. The clauses in the construction contract set out how these claims are to be dealt as they arise.

In order to be entitled to claim, it is stipulated in most standard forms of building contract a prerequisite procedure of notice of intention to claim. The notice of intention to claim or the notice to claim (NTC) is known for a fact as one of essentials to claiming and must be in a written form. NTCs must specify the default or reason for issuing the notice, to whom must the notice must be sent, the duration up until when it is valid to send the NTC, and the proper service of sending the NTC.

¹ Cl. 11.7 of PAM Standard Form of Contract 2006 (With Quantities)

² Cl. 23.1 of PAM Standard Form of Contract 2006 (With Quantities)

³ Cl. 24.1 of PAM Standard Form of Contract 2006 (With Quantities)

⁴ Cl. 22.1 of PAM Standard Form of Contract 2006 (With Quantities)

Failure to meet any of the conditions mentioned may bar the claimant to be compensated.

The issue of a notice being a condition precedent for claim entitlement often disregarded by a claimant. In cases where such requirement was not complied into, it would usually amount to the party waiving his rights to claim and eventually disentitle himself to make a claim. This is illustrated in the case of *Ho Pak Kim Realty Co Pte Ltd v Revitech Pte Ltd*⁵, that was decided by the High Court in Singapore. The clause 23(2) of the contract provides that:

"It shall be a condition precedent to an extension of time by the Architect under any provision of this Contract including the present clause (unless the Architect has already informed the Contractor of his willingness to grant an extension of time) that the Contractor shall within 28 days notify the Architect in writing of any event or direction or instruction which he considers entitles him to an extension of time, together with a short statement of the reasons why the delay to completion will result."

The learned judge to the case decided that the plain meaning of the clause should be upheld and failure of the contractor to comply with the requirements disentitled him to being awarded with an extension of time (EOT).

And since failure to comply with NTC requirement as in the above case makes it impossible to claim, the question of claim entitlement arises in such cases, for example, where the contractor did preserve his rights in claiming until such time when the change order is executed or when complete and full particulars to the claim are available.

⁵ [2010] SGHC 106

In order to impose the rights stipulated within the construction contract, it is therefore important to provide a constant and clear notice reminder once a construction claim is perceived. Aside from the formal notice to claim, contractors in most cases, without knowing its implication, are always opting for the easiest way in achieving entitlement, which is reserving their rights to claim.

Twomey (2016) explained that in American legal practice, reservation of rights (ROR) is a statement that one intentionally retaining his full rights, so as to warn the others of those rights. This ROR notice prevents future claims that may be waived legal rights that were held under a contract, a copyright law, or any other applicable law.

Under the Uniform Commercial Code⁶, a party who with explicit reservation of rights performs or promises performance or assents to performance in a manner demanded or offered by the other party does not thereby prejudice the rights reserved⁷.

In relation to construction industry, this occurs when a contractor who was issued with an instruction to do a variation order (VO), submits a proposal of the work, and anticipates that there may be costs other than direct cost or a delay may be suffered, he then would reserve the right to claim for these unforeseen events and accumulative impacts, and subsequently comply to the performance or acceptance of the work under the ROR.

However, it may be concurrent to infer similarly that when a contractor signs a change order (CO) to be completed, the signature usually acknowledges that *full*

⁶ Uniform Commercial Code is a statutory contract law created by National Conference of Commissioners on Uniform State Law. It was developed to create a uniform standard of practice in commercial law, and often modifies the common law contracts. (Tepper, P. (2014). *The Law of Contract and the Uniform Commercial Code*. 3rd Edition. Cengage Learning. pp.9, 15)

⁷ Uniform Commercial Code § 1-308 (formally 1-207). Retrieved from <http://www.freedom-school.com/law/ucc-1-308-reservation-of-rights.html?cv=1>

*accord and satisfaction*⁸ is being received in both time and money for both time and money for the cost and the effects of the change. This renders that no further claims may be asserted in the future.

There remains to be an argument whether the full accord and satisfaction language supersedes the reservation of right language in terms of claim entitlement.

Nevertheless, ROR is used most of the time to say that “*Yes, I will claim but would like to take the time to gather as much proof as I can without waiving my rights*”. The party then, upon reserving his rights, is given the perception that he has mentioned of his intention and is relieved of the “*time is of the essence*” provision in submitting his full supporting documents. It is becoming evident nowadays that a party used to reserve his rights for future action but how sure is he of his entitlement to claim is preserved that way.

ROR can be submitted as an addition or as an alternative to the notice to claim by way of a separate letter or may be added as a statement in the NTC.

For instance, in PAM 2006 Standard Form of Contract of Malaysia, clauses for NTC is clearly a condition precedent to claim for work done due to instructed VO but it is peculiar to send an NTC every time a contractor is issued with an Architect’s Instruction (AI). Hence, some contractors would elect to use ROR to claim upon receipt of each of the of the instruction because generally, contractors can only determine the estimated direct cost of the VO in his submission of the NTC but indirect impacts are difficult to ascertain in the same instant. This occurrence is better illustrated in the case of *Perbadanan Pemabangunan Pulau Pinang v Trikkon Construction Sdn Bhd*⁹ whereby the contractor has reserved his rights to claim in the future, every time he has received an instruction to do a VO. It is believed that the best

⁸ ‘accord’ meaning agreement and ‘satisfaction’ meaning consideration. The foregoing of the existing rights under the contract will amount to good consideration for the promise to release the other party from his or her obligation. (Stone, R. (2013). *The Modern Law of Contract*. Routledge. p. 115)

⁹ [2012] 2 MLJ 28

chances of entitlement for the perceived unknown cost and time delay is thru reserving his rights to claim for uncertain indirect costs and/or time extension. This approach referred by Singh (2007) and is popularly known as the two-stage approach of claiming whereby, first, contractor is to make an initial application containing information of the heads and amount claimed and subsequently provide documentary evidence and full particular of claim within the stipulated time stated in the standard form of construction contract being used.

In this so-called two-stage approach, the applicant, having the intention to claim, would incorporate in his initial application the ROR statement which could signify to his acceptance of doing work and abiding on the contract provisions but at the same time maintains and keeps his right to be entitled of the unknown impacts in execution of the works, may it be a monetary, time and other additional claims for occurrences that is not covered in the original contract. Furthermore, it is serves as a reminder to the other party that the applicant should not be barred from asserting his claim while the period of claiming has elapsed, and the rights to claim remains to be in his favour.

One of the most common disputes in construction arbitration is whether the claim notice provides adequate notice of secondary or cumulative costs.¹⁰

According to this theory of recovery, “*the issuance of an unreasonable number [or unusual kind] of change orders creates a synergistic disruptive impact such that the total disruption caused by the changes exceeds the sum of the disruptive impacts caused by the individual change orders when looked at independently.*”¹¹

This type of construction claims especially in relation to claiming numerous VOs, which are normally due to design problems and owner’s request, are becoming a headache to contractors. As much as possible, contractors would like to protest the requirement to perform extra work unless the price is right due to VOs may obstruct

¹⁰ Permesley, J. and Cohen, T. (2016). International Arbitration Involving Construction: Best Practices for Documenting Claims and Defenses. Retrieved from <http://us.practicallaw.com/w-001-4134>

¹¹ Finke, M. (1997). Claims for Construction Productivity Losses. 26 Pub. Cont. L.J. p.311, 317.

their originally planned schedule and resources from being completed on time and on budget. For that reason, in order to keep their right to be entitled to the cost and time impact, it is becoming a practice to include a ROR statement to every AI / EI they would receive as part of their NTC. It said to be a contractor's way of prompting that as a result of the VO to be done, claims (i.e. delays, disruption of regular work progress, cumulative claim impact to direct and indirect costs) both foreseen and unforeseen may be incurred and that the rights to claiming are reserved until the works are completed and final assessment is performed.

This is becoming a practice due to circumstances where the contractor is only certified of the direct costs and time incurred due to the VO, however, other impacts that may only be assessed at the end of the project, such as the ripple effect of numerous VOs done by the contractor are often taken for granted. The provision of the contract may not particularly state how claims of this kind may be addressed thus, ROR is important for contractors not to release its rights to receive compensation for all its perceived extra cost.

Aside from ROR in claiming for costs, extension of time and direct loss and/or expense, ROR is also used in occasions such as, ROR to terminate the contract where contractor does not comply to notice of default, ROR to commence arbitration proceedings, ROR impose liquidated damages and so on. However, this study shall be concentrating on ROR to construction claims.

In any case, ROR statements may be advantageous for a party asserting his claims, provided that it is worded and done in rightful manner. The contract being used may also be a component to the success of the party preserving his rights. Other conditions of imposing the right to claim may be established based on the cases.

It is therefore valuable for us to review, understand, analyze and evaluate the usage and the reasons, in reference to court decisions, for judges' deliberation for upholding or denying the application for ROR in Construction Claims.

1.2 Problem Statement

The standpoint of a claimant who reserved his right maybe viewed in two situations. First, where the claimant has issued an NTC and has reserved the right to claim. This saves the claimant a lot of trouble since he had doubled his defenses and increased his chances in obtaining the claim. Claimant continue to utilize the ROR statement, in this situation, since there are cases that NTC may not be sufficient to cover the expenditures (i.e. delay cost, impacts of numerous instructions, standby of equipment fees, additional preliminaries) that might be incurred. Further, time incurred due to the change order is difficult to put an initial estimate thereby contractors would include “*reserving the rights to claims for an EOT if the need may arise*” statement to ensure that the contract administrator has the knowledge of his intention. In a more precise example, a contractor may notify the owner that it has incurred certain cost overruns or request an extension of time to complete a specific task, but it may not be in a position to quantify the particular long-term effects of the impact on productivity. In these circumstances, the contractor should highlight the potential for long-term cumulative effects and reserve its right to claim those costs or additional time later.¹²

Second, where claimant missed out the NTC requirement but has reserved the right to claim. In this particular instant, it might be said that failure of complying to the NTC precondition would definitely lose the entitlement to claim, but some court decision has given the weight to the ROR statement of the claimant.¹³ Sweet and Schneier (2008) also mentioned that when the owner was aware of the additional work and made no objection to it, the doctrine of waiver may be applied to oppose the notice requirement. Entitlement may still be possible and this is kept in line with Bramble and Callahan (2010) explaining that there is a need for the contractor to explicitly reserve rights to delay and disruption claims arising out of change orders. The authors

¹² Permesly, J. and Cohen T. (2016). International Arbitration Involving Construction: Best Practices for Documenting Claims and Defenses. United States: Practical Law TM.

¹³ see Gainesville-Alachua County Reg'l Airport Authority v R. Hyden Const., Inc 766 So. 2s 1238 (1st Dist. 2000)

added that when executing a change order, if the contractor expressly reserves its rights to recover delay costs arising out of the change order, it may later recover those costs.

The good illustration to the point is the case of *Perbadanan Pembangunan Pulau Pinang*¹⁴. The Court of Appeal's decision opposes the earlier decision of the arbitrator in regard to claims, where the contractor has reserved their rights and was decided to be entitled to compensation. The arbitrator further asserts that the use of the two-stage approach be upheld but was eventually set aside by the higher authority (Court of Appeal) due to the notice including the ROR did not contain any quantum of claim as specified in the contract clause which inhibits the mere ROR to succeed.

However, the case of *Sa Shee (Sarawak) Sdn Bhd v Sejadu Sdn Bhd*¹⁵ has formed a different view to ROR. The learned judge to the case had not only given weight but also relied to the ROR in his decision in awarding the damages to the claimant due to the ROR had been secured beforehand. This case may be supported by Callahan's statement that that "an express, clear reservation of rights can successfully allow the contractor the ability to claim additional delay damages in the future".

Both cases have included their ROR statements as being part of their NTC to the other party. Although circumstances to which they were applied is distinctive, principles to which they were upheld and denied are good points of study.

The research is to provide greater understanding of these issues to construction claims having ROR statements in regard to its legal implications based on the arbitrators' and judges' standpoint to which the claim was denied and upheld.

¹⁴ *supra*

¹⁵ [2000] 5 MLJ 414

1.3 Research Objective

The main objective of this research is to determine the principles used by judges in denying or upholding the “*Reservation of Rights*” in construction claims.

1.4 Scope and Limitation of the Study

The study focuses on ROR in construction claims, but is not limited to, direct and indirect costs for variation, extension of time, direct loss and/or expense and liquidated damages. However, cases which relates to insurance will not form part of the research.

Due to ROR is uncommon to Malaysian jurisdiction and is more prevalent in American jurisdiction, there will be no jurisdictional limitations provided that the case is relevant to the ROR in building contracts.

1.5 Significance of the Study

The study aims to advise contracting parties in construction agreement regarding their entitlement to claim for any time and cost impact upon reserving their rights to claim. The research also intends to determine whether a party intending to claim may continuously rely on ROR statement in reference to legal cases or should cease leaning towards the use of ROR statements. Furthermore, this study aims to give emphasis of the differences and significance of the notices from the ROR statements.

1.6 Research Methodology

In order to systematically achieve the objective of the research, it is vital to lay down the guidelines to the process and method of accomplishing the study. Basically, this research process is comprised of four major stages which involves the following:

1.6.1 Initial Study for Finding the Research Topic, Objective, Scope and Outline

The first stage of doing the initial study involves reading articles, recent legal cases and journal of research area which interests the researcher. A discussion to friends and lecturers in order to obtain suggestive topics, narrowing down and determine a research topic. After the initial readings and study, the objective and scope of the research is to be properly identified. From then, a research outline is to be prepared in order to identify the preliminary and secondary data and references to obtain as needed for the project.

1.6.2 Collecting Data and Sorting the Data Obtained

Collection of all relevant data and information is done during this second stage. Primary data are mainly from the books, journals, e-news letters and articles from authoritative publishers and professional bodies, while the legal cases will be taken mainly from the Lexis-Nexis online database, law journals and other electronic resources. All the cases relating to the research topic will be sorted out from the database. The cases that are mostly relevant in achieving the objective will be collected and used for the analysis at the later stage.

1.6.3 Data Analysis and Interpretation

The third stage involves arrangement, reading, understanding and interpreting the relevant data collected. This process also requires the researcher to digest all the readings to come up with the literature review and analyze the legal cases for correct interpretation and construal of the judges' decision.

1.6.4 Writing-up and Conclusion

This stage is the final stage of the research process. It involves mainly the writing up and checking of the writing. Part of this stage is delivering the conclusion and recommendations based on the findings based from the analysis of the data.

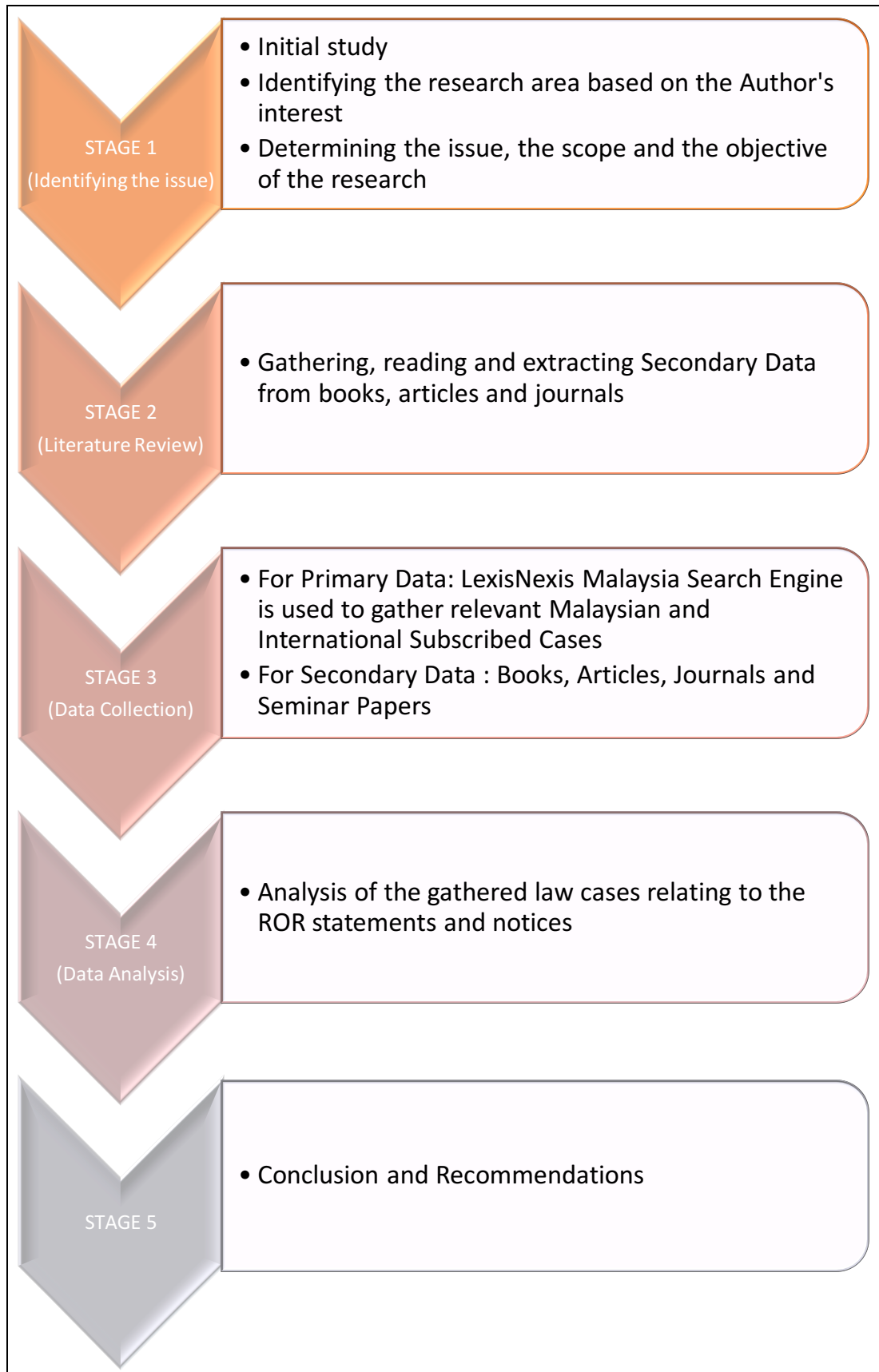


Figure 1.1 Research Methodology

As part of the research methodology case finding, the process of obtaining the cases are summarized in the table below:

Table 1.1 Searching Hits for ROR Cases in Lexis Malaysia®

Search Term No.	Keywords	Results
Lexis® Malaysia > Cases > International Cases > Sources: All Subscribed Cases Sources		
Search Terms 1:	reservation of right and construction and notice and change order	6 Hits > 3 Cases
Search Terms 2:	reservation of right and construction and notice and variation order	6 Hits > 3 Cases
Search Terms 3:	reservation of right and building and notice and variation order	2 Hits > 1 Case
Search Terms 4:	reservation of right and building and notice and change order	5 Hits > 2 Cases
Search Terms 5:	reserved their right to claim and construction and notice	6 Hits > 4 Cases
Lexis® Malaysia > Cases > Sources: All Subscribed Malaysian Cases Sources		
Search Terms 1:	reservation of right and construction and notice and change order	No documents found
Search Terms 2:	reservation of right and construction and notice and variation order	3 Hits > 2 Cases
Search Terms 3:	reservation of right and building and notice and variation order	3 Hits > 2 Case
Search Terms 4:	reservation of right and building and notice and change order	No documents found
Search Terms 5:	reserved their right and building and notice	15 Hits
Search Terms 6:	reserved their right to claim and construction and notice	3 Hits > 3 Cases

The table shows the search outcomes made from Lexis Malaysia, the researcher revolved around the similar keywords in order to obtain more relevant cases. It may be shown that there are 6 hits yet only 3 cases have been identified, this is due to the case has been reported to different law journals. The option of choosing which case is referred is based on which one has discussed in a more detailed manner about ROR statement.

1.7 Organisation of the Report

The study covers five (5) chapters as follows:

Chapter 1: Introduction

This chapter aims to give a preview of the whole report through the background of the study, problem statement, objective of the study, scope and limitation of the study, significance of the study, research methodology and the organisation of the chapters.

Chapter 2: Construction Claims, Notices and Procedure in Claiming

Chapter 2 discusses the basic terminologies and provide a general understanding of different types of claim in construction and the claiming procedures as referred to the Malaysian Standard Forms of Construction Contract. A brief and general understanding of how American procedures

claims are being done is included. Readers will also be enlightened regarding NTC conditions and NTC as a condition precedent.

Chapter 3: Reservation of Rights

This chapter discusses the basic terminologies and provide a general understanding of ROR statements in construction claims which will be useful in reading the subsequent chapter. Part of this chapter would be about examining the ROR Statements' wordings as used by a party in preserving its right to claim in a superficial basis as to the wordings.

Chapter 4: Legal Implication of Reservation of Rights in Construction Claims

This chapter analyses legal perspective of the entitlement of a party to claim upon reserving its rights to obtain compensation, in order to achieve the objective of this project report. The author refers to the various court cases of law journal and law reports, i.e. Malayan Law Journal, All England Report, Canada Law Report, Building Law Report, Construction Law Report.

Chapter 5: Conclusion and Recommendations

This final chapter summarizes the findings of the research analysis, the problems and obstacles encountered during the research and the recommendations for future researches.

1.8 Conclusion

This chapter discussed in summary the contents of the research project, the process of obtaining the primary and secondary, analysing and interpreting the data and the results and finally concluding the outcome of the research. The prevalent use ROR statements as a form of NTC formed as an initial point of the reason of the study. The question of whether the ROR statement may be considered good as a NTC is to be the main purpose of the study in order to guide construction industry players in the usage of the ROR statements.

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