



Method of Valuing Variations Under Construction Contracts.

“In the ICE Conditions the contractual foundation for the rule that the rates and prices are immutable even though they prove to be too profitable or uneconomic”

His Honour Judge Humphrey LLOYD QC

Whether it's during the contract period or at the final account stage, it is not uncommon that construction disagreements and disputes often relate to contract variations and in particular, the method by which the variation is valued. Indeed, whilst recent research¹ shows historically adjudications relating to value of work and variations amount to 20% of all adjudications, the recent decrease is masked by the significant increase in withholding and payless disputes, which may well include unagreed amounts relating to variations.

Disagreement as to the value of variations occur for several reasons not least, the actual cost of the variation is greater than the perceived value returned, the works are undertaken in different circumstances than the planned scope of works, the timing and conditions of the varied work is undertaken is inconsistent with the contract scope of works by which the works were priced and or the conditions of contract have been misinterpreted or misunderstood.

¹ Report No.14, Adjudication Reporting Centre in conjunction with The Adjudication Society April 2016



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Indeed, this final point was highlighted by HH Judge Humphrey Lloyd²:

“That the type of question raised by this appeal is a matter of the construction of the contract (here clause 52(1)) and not a question of valuation or fact”.

Where there is no agreement to the value of variations, standard form contracts, including JCT, ICE and CECA³ have their own specific mechanisms for valuing additional, omissions or substituted work. Notwithstanding this, where a contract provides specific valuation rules for valuing variations, disputes can still arise relating to which valuation rule applies and how the rule is interpreted.

Essentially, the methods of valuation consider whether:

1. Contract bills of quantities or schedule of rates are applicable to the varied works.

² Henry Boot Construction Ltd v. Alstom Combined Cycles [1999] EWHC Technology 263

³ Joint Contracts Tribunal Standard Building Contract, Infrastructure Conditions of Contract and Civil Engineering Contractors Association Form of Sub Contract



2. Whether the varied work was of similar character and nature to those in the contract bills,
3. Are the works undertaken in similar conditions as those proposed in the contract bills; and
4. Are there significant variances in the quantity of work, as set out in the contract bills.

During the tender process, the production of rates and the pricing often lack the foresight that in the event of variations occurring they will be used as a basis for valuation. Contract bills will be used either for the method by which variations are to be valued or the basis for the valuation, making allowances for the change in conditions or character. The use of contract bill rates as the basis of valuing variation is often a contentious issue as the dissenting party may argue that the component parts of the rate are only applicable to the rate for the specific applicable item in the contract bills.

Where errors in the contract bills have subsequently been established, this cannot be used as a defence from using the rate to value variations. In *Henry Boot v Alstom Combined Cycles*⁴, the contract was ICE Condition of Contract⁵, the contractor included a contract bill item for temporary sheet piling, the rate was subsequently proved to be erroneous. Further sheet piling was subsequently instructed in a different location of the site, which when assessed using the contract bill rate resulted in a 'windfall gain' in the Contractor's favour.

In a decision upheld in the Court of Appeal⁶, the judge decided that the use of contract rates is absolute and are not to be adjusted even if it is subsequently established they are erroneous:

"Clause 55(2) does no more than restate (in a place where it may be particularly apposite) the fundamental proposition that the contract rates and prices are sacrosanct and not subject to correction. In the ICE Conditions the contractual foundation for the rule that the rates and prices are immutable even though they prove to be too profitable or uneconomic....."

Notwithstanding the facts, contract rates are to be used as the basis of the valuation of the variation where the character or conditions may be different to those in the contract bills. This was further confirmed by the judge in *Henry Boot*⁷:

"If the varied work is work of a dissimilar character or to be executed under dissimilar conditions, then the contract clearly maintains the principle that a valuation ought to be made if there is a contract rate or price applicable or which could be used as a basis for valuing the variation".

⁴ Henry Boot Construction Ltd v. Alstom Combined Cycles [1999] EWHC Technology 263

⁵ ICE Conditions of Contract 6th Ed

⁶ Henry Boot Construction Ltd v. Alstom Combined Cycles [2000] EWCS Civ 99

⁷ Ibid



It has been suggested, that this approach may be questionable⁸:

“Whilst the inflated rate for the work contracted for cannot be adjusted, it seems less clear why it should be reasonable to apply such a miscalculation to varied work which is not of a similar character. This is on the simple ground that it is not reasonable to apply a rate which obviously overcompensates the Contractor for the work done and would lend encouragement to the sort of rate manipulation where the Contractor is encouraged effectively to gamble on the necessity for additional work where the applicable rates have been deliberately inflated.”

However, whether the rate is reasonable to use was addressed by Lord Justice Ward in the Henry Boot appeal⁹, where he stated:

“reasonableness is determined by, and is solely dependent upon, whether the varied work is reasonably sufficiently similar to the contract work to justify the use of contract rates.”

Similar Conditions may vary from one work element to another and the circumstances will be dependent on the demonstration of the facts surrounding the variation in question. However, *Keating on Construction Contracts*¹⁰ suggests:

“Dissimilar conditions might, it is suggested, include physical site conditions such as wet compared with dry, high compared with low, confined space compared with ample working space and winter working compared with summer working, where the Contract Documents show that the Bill prices were based on such conditions.”

Further consideration should also be given as to the programming and timing of when the work was undertaken, as if delays occur and the contractor is deemed culpable for the delays then it may be considered that had the contractor delays not occurred the variations may have been instructed earlier and the change in conditions may not have happened.

A significant change in the quantities may also give rise to a change to the contract rates as a significant reduction in quantities may result in a loss through inefficiencies and equally, a significant increase may result in improved economies of scale. Both the JCT SBC under clause 5.6 and the ICC under clause 56 (2) address the issue of where the actual quantities are greater or lesser than the contract bills, rendering the contract bill rate inappropriate.

⁸ Hudson’s Building and Engineering Contracts 12th edition 5-014.

⁹ Henry Boot Construction Ltd v. Alstom Combined Cycles [2000] EWCS Civ 99

¹⁰ 9th Edition (2012) paragraph 20-305



In the absence of being able to use the contract rates and prices either as a rate or the basis of a suitable rate, fair rates and prices are a valid mechanism to value variations.

The judge in *Henry Boot*, was clear to set out the alternative to contract rates or as amended:

“A fair valuation when used as an alternative to a valuation by or by reference to contract rates and prices generally means a valuation which will not give the contractor more than his actual costs reasonably and necessarily incurred plus similar allowances for overheads and profit for anything more would confer on him an additional margin for profit and would not be fair to the employer.”¹¹

In *Weldon Plant v The Commission for New Towns*¹², HH Judge Humphrey Lloyd, again addressed the issue of a fair valuation which would be based on actual costs reasonably and properly incurred:

“the contractor would be entitled to a fair valuation which would ordinarily be based upon the reasonable costs of carrying out the work, if reasonably and properly incurred Clearly if, in the execution of the work, cost or expenditure is

incurred which would not have been incurred by a reasonably competent contractor in the same or similar circumstances, then such costs would not form part of a fair valuation.”

Furthermore, in this instance specifically whether profit forms part of a fair valuation, he said:

“Indeed in my judgement a fair valuation must, in the absence of special circumstances (none of which have been identified by the arbitrator), include an element on account of profit. a contractor is in business to make a profit on the costs of deploying its resources,”

Often parties’ opinions on the principles of how variations are valued differ however, as it has been identified above, it is essential when valuing variations to firstly analyse and understand the contractual mechanism by which variations are valued, under the specific contract conditions. On assessing the contract valuation rules, it is then that one should look at the facts in question to establish the method of valuation set against the factual background and the resulting outcome of the valuation.

By undertaking an analytical approach to understanding and interpreting the construction of the contract, set against the facts in hand, this will go some way to improve the agreement the valuation of the variations, settlement final accounts and ultimately avoid timely and costly disputes.

¹¹ *Henry Boot Construction Ltd v. Alstom Combined Cycles* [1999] EWHC Technology 263

¹² *Weldon Plant Limited v The Commission for New Towns* [2000] EWHC 76 (TCC)