LEGAL ISSUES OF PARTNERING IN CONSTRUCTION INDUSTRY: MALAYSIA CONTRACT LAW SYSTEM

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Partnering is gaining popularity as an innovative method to carry out construction projects globally. It is a concept that provides a framework for the establishment of mutual objectives among the building team members with an attempt to reach an agreed dispute resolution procedure as well as encouraging the principle of continuous improvement. Though it has been debated that, partnering is not about contracts, there are legal issues to be considered in the adoption of partnering concept. The aim of this research is to fill in the existing gap in the legal issues of partnering in the construction industry. The research focuses on the analysis of legal issues of partnering in the construction industry and also to determine the appropriateness of partnering term which suits the nature of Malaysia’s construction industry. It highlights the definitions of partnering in the construction industry, the research objectives and the research methodology. Also, from the methodology of literature review and case law reviews several legal issues of partnering in construction industry are derived which cover the interpretation of contractual documents, principle of good faith, fiduciary relations, doctrine of estoppel and waiver and misrepresentations. The ultimate aim of this research is to produce a framework of the partnering contract which is suitable for the Malaysian construction industry and to serve as a reference in the implementation of partnering in Malaysia.

Keywords: construction projects, legal issues, Malaysia, partnering.

INTRODUCTION

Dispute resolution has become an ordinary characteristic of the usual construction project process (Cornick et al. 1999). Normally, the building team members make decisions based on their own goal and objectives without considering the impact on the other party. This can lead to an adversarial relationship. Various studies agree that this situation significantly affect the productivity and efficiency of the construction industry (Kadefors 2004; Scott 2001). Consequently, this relationship has contributed to the need for a better approach, and one of it is partnering; which is an innovative concept to construction organizations, which traditionally rely heavily on contracting to bind the parties together (Cheng and Li 2004). The formal introduction of partnering into the Malaysian Construction Industry was done in 2007 through the Construction Industry Master Plan (CIMP), but before this, in 2000, a joint seminar on project based partnering in Public Works Department (PWD) was organized by the

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department and the Master Builders Association Malaysia titled “Introducing the Concept of Partnering in the Construction Industry”.

DEFINING THE PARTNERING IN CONSTRUCTION INDUSTRY

The Construction Industry Institute (CII) in the United States of America defined partnering as: “A long-term commitment between two or more organizations for the purposes of achieving specific business objectives by maximizing the effectiveness of each participant resources. This requires changing traditional relationship to develop a shared culture without regard to organizational boundaries. This relationship is based on trust, dedication to common goals and an understanding of each other’s individual expectations and values.” (CII 1991).

RESEARCH OBJECTIVES

Partnering is the opportunity for participants to share in the rewards of improved performance (CIDB 2007). Hence, for the concept to be put into practice, it is practically important to conduct studies regarding various issues of partnering so that it will act as a reference in the future. It fills a void that has not been studied, while most of the studies were focusing on the implementation critical success factors and barriers of partnering, there is less studies related to legal issues of partnering. There are three objectives in this research as listed below.

1. To examine the legal and contractual issues that arises from the adoption of partnering concept in construction industry.
2. To determine the appropriateness of partnering terms that suits the nature of Malaysia’s construction industry.
3. To produce framework of the partnering contract that is suitable for the construction industry in Malaysia.

RESEARCH METHOD

In order to address the first objective that is mainly discussed in this paper, that is to examine the legal and contractual issues that arise from the adoption of partnering concept in construction industry, in-depth literature review and case law analysis will be conducted. Through the literature review and case law analysis, the concept, ideas or theories in respect of any matter related to legal in partnering will be examined and identified. The sources will covered the construction law journal, Malayan law journal, lexis nexis, articles, reports and books.

ASSOCIATED LEGAL ISSUES AND DISCUSSION

According to Lyon (1995), any time new business relationships are formed, it can be anticipated that the legal components of such relationships must inevitably develop. In view of this, the notion that partnering has no legal consequences is open to challenge. Where appropriate, references were made to legislation and reported cases so as to illustrate the relevant legal principles.

Interpretation of contractual documents

The impact of partnering arrangements on formal contract undertakings is illustrated in the recent decision of Judge Humphrey Lloyd in Birse Construction Ltd v. St. David Limited [1999]. The brief facts of this case are as follows: the contractor, Birse, carried out for the employer, St David some of the work required for the construction of luxury apartments. A “Team Building Seminar” took place at which both parties signed a Charter, basically the Charter stated the main objective that to produce an
exceptional quality development within the agreed time frame, at least cost, enhancing our reputations through mutual co-operation and trust. The overall contract period, contract programme and various preliminary costs were discussed and agreed between the parties. St David sent the draft contract documents based upon JCT 80 to Birse who neither signed nor returned the documents. Over the following months, St David became unhappy with Birse’s performance. There were discussions on signing of the contract but Birse was reluctant to do so until the contract programme was reviewed and dealt with satisfactorily. Birse then commenced legal proceedings for payment of works done on a quantum meruit basis, arguing that no contract was concluded between the parties. St David applied for a stay of the action pending arbitration, arguing that a contract based upon the JCT 80 form, which included an arbitration agreement, had been made between the parties.

Judge Lloyd examined the history of dealings between the parties and found that there was binding contract between the parties which incorporated the JCT 80 conditions. It appears from the following comments of Judge Lloyd that the partnering charter signed by the parties was a factor which influenced his decision: “The terms of that document (partnering charter), though clearly not legally binding, are important for they were clearly intended to provide the standards by which the parties were to conduct themselves and against which their conduct and attitudes were to be measured.” On the lack of formal documentation, the Judge commented that: “People who have agreed to proceed on the basis of mutual co-operation and trust, are hardly likely at the same time to adopt a rigid attitude as to the formation of a contract.”

Further, he went on to say that: “Even though the terms of the Charter would not alter or affect the terms of the Contract (where they are not incorporated or referred to in the contract or are not binding in law in their own right) an arbitrator (or court) would undoubtedly take such adherence to the Charter into account in exercising the wide discretion to open up, review and revise etc. which is given under the JCT conditions.” Judge Lloyd appeared to take the view that if a party had agreed to co-operate by way of a partnering charter, it could not then go back on its word by failing to co-operate. So, while the partnering agreements are non-binding, it appears open for the courts to take these into account and imply high standards of moral conduct into the contract.

Good faith
The expression good faith makes frequent appearance in contract law (Waddams 1995). However good faith can be used in different contexts with different meanings. Rather, good faith is a concept capable of both enlarging and restricting contractual obligations. In the USA, and the latest legal development there, recognizes contracts, do include a principle of good faith (Newman 2000). The Associated General Contractors of USA (AGC) described: “Partnering is not a contract, but recognition that every contract includes an implied covenant of good faith.” It has been said that, partnering does not replace a construction contract, but it does at least “enable it to be administrated on a more harmonious basis” (AGC 1991). This idea also appears in the Defence Construction Canada (1999): “Partnering a project does not change the contract, but does help all parties to recognize that the requirement to act in good faith is a basic tenet of contract law”. Partnering necessarily imports the concepts of ‘good faith’ and ‘fair dealing’.

In Walford and others v Miles and another [1992], Lord Ackner stated, “An agreement to negotiate has no legal content” and “good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations”. However,
according to Colledge (2000), the courts have in recent decisions moved significantly toward explicit recognition of an implied obligation of good faith in the performance of contract. In Birse Construction Ltd v. St. David Limited [1999], Justice Humphrey Lloyd stated: “The terms though clearly not legally binding are important, for they were clearly intended to provide the standard by which the parties were to conduct themselves and against which their conduct and attitude were to be measured.” Clearly, some major countries using the common law legal system have already recognized “good faith”, and even in England, the legal concept of “good faith” is changing to converge with global practice.

**Fiduciary relations**

Parties to a commercial relationship will usually be governed by the terms of their contract and not by superimposed equitable duties. However, the court may impose fiduciary obligations upon parties to a contract if the relationship between them shows that they are putting themselves in a position where they are placing reliance upon each other to act in each other’s interests. The court found that in the well-established categories of relationship in which the fiduciary duty has been held to arise, three general characteristics were evident, first, the fiduciary has scope for the exercise of some discretion or power, second, the fiduciary can unilaterally exercise that power or discretion so as to affect the beneficiary’s legal or practical interest and the beneficiary is peculiarly vulnerable to, or at the mercy of, the fiduciary holding the discretion or power (Ahmad 2002). The Stair Memorial Encyclopaedia (1995) concluded that “partnership is a relationship of good faith, even if not requiring uberrima fides, and it is clear that partners are regarded as being in the position of fiduciaries towards each other”.

Legal partnership is a particularly intense fiduciary relationship and this regard in Helmore v Smith [1886] where the judge stated that “if the fiduciary relation means anything I cannot conceive a stronger case of fiduciary relations that that what exist between partners. Their mutual confidence is the life blood of the concern. It is because they trust one another that they are partners in the first instance; it is because they continue to trust each other that the business goes on.”

**Doctrine of estoppel and waiver.**

Under the common law, consequential damages are those damages that arise from the intervention of special circumstances not ordinarily predictable. Consequential damages fall within what is known as the second limb of Hadley v Baxendale [1854]. As such, consequential damage or loss does not cover loss that directly and naturally resulted from the ordinary course of events. The distinction between direct and consequential damages is often blurred, and this can lead to uncertainty in the quantification of damages (Jones 2002). In order to avoid this confusion and to promote openness between the parties, the American Institute of Architects (AIA) Form A201 (General Conditions of the Contract for Construction) has been amended to include a blanket waiver of consequential damages. The relevant waiver clause (4.3.10) provides that both the contractor and the owner waive claims against each other for consequential damages. This mutual waiver includes on the part of the owner, a waiver damages in respect of “rental expenses, for losses of use, income, profit, financing, business and reputation and for loss of management or employee productivity or of the services of such persons” and; on the part of the contractor, a waiver of damages in respect of “principle office expenses including the compensation of personnel stationed there, for losses of financing, business and
reputation, and for loss of profit except anticipated profit arising directly from the work”.

The changes in the A201 Form are significant and certainly the concept of waiving claims for consequential loss is an innovative approach. The FIDIC provision, clause 17.6 in the new Red Book, only include a short list of consequential loss or damage examples and to this extent could be said not to effectively limit each party’s potential liability for consequential loss or damage. Similarly, creative quantification of direct damages can also be used to frustrate the purpose of such clauses. Nevertheless, as with partnering, the acceptance of this approach ultimately hinges on a change in mindset between the stakeholders (Jones 2002). This change in mindset was recognized and encouraged by the Tang’s Report (Tang 2001) where reference was made to the need for a “new culture in the construction industry”. Unless the parties to the construction contract regard themselves as ‘partners’ instead of ‘adversaries’, they are unlikely to be able to mutually relinquish their entitlement to claim consequential damages.

**Misrepresentation**

When a statement made during negotiations leading to a contract is deemed not a term of the contract or a warranty collateral to the contract, it is a ‘representation’. Such pre-contractual statements, though not intended to have contractual effect, may have seriously affected the inclination of one party to enter into the contract. If the representation is false, the party misled cannot claim damages for breach of contract because no term of the contract has been broken. However, the party misled may claim relief accorded by the law for misrepresentation. In case of P Ward v Civil and Civic [1999], a dispute arose over payment for the costs of design carried out by Ward during the course of the Subcontract. Ward claimed that Civil and Civic had represented to them the partnering relationship between them “would be in the nature of a partnership and that they would co-operate to ensure that the project was a financial success for both the Plaintiff and the defendant”, and that in this context Civil and Civic’s failure to draw Ward’s attention to the changed liabilities amounted to misrepresentation.

However the judge advised that “the most obvious of the difficulties is the fact that Ward seeks to disavow a formal written contract signed by both parties following close dealing between them over a period of almost a year, which dealings were, on my findings, clearly understood by both parties as intended to culminate in the execution of the Subcontract”. Although, the Judge dismissed the partnering aspect in this case, it shows that this issue can arise in adopting partnering in construction industry. In other case, Thiess Contractors Pty Ltd v Placer (Granny Smith) Pty Ltd [1999], the Judge found that during the pre-contract negotiations the parties were at ‘arms length’ and was not persuaded that the relationship between Thiess and Placer up to the point at which they entered into the contract, was a fiduciary one. He considered that “there has been a misrepresentation: not a breach of fiduciary duty”. Given the wide ambit of the Misrepresentation Ordinance, it is foreseeable that disenchantled participants in partnering will seek to assert that, the representations made in the course of the process amounted to misrepresentation conduct (Jamieson, 2001).
Discussion of the legal issues
This section will discuss further the legal issues in partnering as explained before. As always, these issues will be of much concern in the event that the relationship between the parties breaks down and disputes arise.

Interpretation of contractual documents
Will the mere presence of a partnering arrangement existing alongside a contract cause the process of interpretation of the terms of the contract to be affected in any manner? Following Birse’s case, the courts may now use provisions of a non-binding partnering agreement to interpret the contractual terms of the parties under the substantive construction contract. It is established that although it is not open to look at parties’ subjective intentions, regard can be had to the ‘matrix of fact’ or the factual background in interpreting the terms of contract. The principles of interpretation were summarized by Lord Hoffman in the recent House of Lords decision of Investors Compensation Scheme Ltd v West Bromwich Building Society [1998] 1 WLR 896 as follows.

1. Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.
2. Subject to the requirement that it should have been reasonably available to the parties and to the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.
3. The law excludes from the admissible background the previous negotiations of the parties and their declaration of subjective intent.
4. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax.

It is likely that a partnering agreement may be considered as a component of this ‘background’ as it is a document which should have been reasonably available to the parties and does not fall within the two exceptions enunciated by Lord Hoffman, i.e. previous negotiations and declarations of subjective intent, as it embodies the mutual commitments made by the parties. Thus, the terms of partnering charter may have a bearing on the meaning of the word ‘reasonable’ satisfaction of the architect or engineer.

Good faith
Will the very presence of a partnering arrangement existing alongside a contract cause to be implied a positive duty on the parties to perform the contract in good faith? It may be argued that a duty to act in good faith is implied into the contract by the parties’ decision to employ the partnering arrangement which in itself is based on principle of good faith-mutual trust and objectives, open communication, honesty, confidence and dispute minimization. Further, partnering is a concept developed and imported from the United States of America which recognizes the doctrine of good faith in contract law.

There is thus far no recognized general duty to perform contractual obligation in good faith in Malaysia or English law (Lucke 1987; O’Byrne 1995; Renard Construction (ME) Pty Ltd v Minister for Public Works [1992] 26 NSWLR 234). There are
however instances of judicial observations, for example in Chay Chong Hwa and Ors v Seah Mary [1984] 2 MLJ 251 that a discretions should not be exercised in bad faith, on the basis that there is a negative duty not to act in bad faith as opposed to a positive duty to act in good faith. In order to establish the potential for good faith obligations in partnering, the nature of the agreement between the parties and the context in which this operates need to be discussed through the familiar techniques of construction of the contract, express terms and implication of a term, to investigate the existence of good faith in partnering. In expressed terms, binding partnering agreement will sometimes include an express general obligation on the parties to act in a good faith. In extreme cases the charter may comprise the contract or may be held to be incorporated by reference. However, given the absence of a uniform statutory or common law definition of good faith under English Law it is unclear how such express obligations would be interpreted. Case law provides limited guidance as to the likely approach of a court when construing express or implied obligations to use good faith and to co-operate in the context of a partnering agreement (Roe and Jenkins 2003).

In attempt to avoid such a situation, care needs to be taken in the drafting of express duties of good faith. For implied terms, the existence of a non-binding charter that includes a joint commitment to co-operate and act in good faith may encourage the court to imply such obligations in the contract. It is unclear whether any such implied obligation would go beyond an obligation to act fairly and reasonably and not to impede or prevent performance by the other party. From law case review, it is clear that the courts are not usually willing to imply a duty to act in good faith except for ‘special relationship’ cases such as insurance. The conclusion emerges that obligation of good faith are likely to be upheld only given the right circumstances. Good faith obligations may arise either as express contract provisions or implied by fact or law.

Fiduciary relations
Fiduciary obligations, effectively, oblige on each party a duty to act in the best interests of the other parties to whom the obligations are owed. These are not typical in a normal commercial relationship but they can be applied in a true partnership such as joint venture agreement. Consequently, a party under a fiduciary obligation must avoid any conflicts between its duty to others and its own self-interest and it must not misuse its fiduciary position for personal gains. Generally, parties to an ordinary commercial contract owe no fiduciary obligations to each other. However, owing to the very nature of partnering agreement, which is based on principle of trust, fairness and mutual co-operation for the benefit of the project, it is arguable that parties have put themselves in a position where they are placing reliance upon each other to act in each other's interest.

The parties to a partnering arrangement must consider whether, just as in the case of joint ventures, they owe fiduciary obligations to each other which impinge upon their freedom to act in their own self-interest (Jamieson 2001). Parties who wish to avoid the consequences of fiduciary obligations should do so by express provisions in the partnering charter. A provision could be inserted to totally exclude the possibility of those obligations from arising. Alternatively, if the participants decide that fiduciary obligations are consistent with the spirit of the agreement, the charter could define the scope of the obligations for the purposes of the partnering process.
Doctrine of estoppel and waiver
It is a reality that in partnering agreement, parties may make charter to one another which do not conform to the contract but upon which they rely. This approach may minimize disputes and increases efficiency. However, if the partnering arrangement breakdown, there will be inevitably a conflict between the requirements of the contracts and the charter made during the partnering process. Parties then in dispute may then be unable to prosecute their rights under the contract due to the doctrines of estoppel and waiver. This is likely given that, if the partnering process is to be effective, it requires parties to act in a manner consistent with achieving their mutual objectives which often will necessitate behaving in a manner different from that required or anticipated by the contract. Accordingly, parties must take care during the partnering process to ensure that their contractual rights are not compromised.

This problem can be addressed by incorporating into the partnering charter a procedure which is to be followed if a party is to be denied its right to insist upon enforcement in accordance with the contract condition or, alternatively, each agreement which alters the position of the parties should be recorded as an amendment to the contract, with the effect of the amendment being strictly limited to the factual matter being addressed (Jamieson 2001). In this connection, it should be remembered that as an implied term, co-operation as agreed to in partnering agreement may require the client to mitigate the other’s party loss where, for example, the project has overrun. Thus the client may have trust upon himself a pro-active role in mitigation. Some even put forward the expressed mutual waiver clause and provision of consequential damages to waive claims for consequential damages at all.

Misrepresentation
When a statement during negotiations leading to a contract is deemed not a term of the contract or a warranty collateral to the contract, it is a ‘representation’. Such pre-contractual statements, though not intended to have contractual effect, may have seriously affected the inclination of one party to enter into the contract. If the representation is false, the party that was misled cannot claim damages for breach of contract because no term of the contract has been broken. However the misled party may claim relief accorded by the law for misrepresentation or fraud (Wallace 1999). In partnering, the team members rely on information supplied by the other parties, each and every party in the team will provide information where they think useful and important to conduct the construction project.

As the team agreed, any critical problem will be discussed and the team will try to find a suitable solution, basically, to ensure the benefits of the partnering process are maximized, team member will enter into partnering’s relationship on the basis of full and frank disclosure. Problems occurred when the team members did not reveal everything regarding to the project, they might think that the information is not important to be shared, while the other members need to know about it in order to avoid losses. When this situation occurred, it is foreseeable that the dizenchanted team members in partnering will seek to involve the course of misrepresentation conduct. It is therefore critically important that the representatives are fully aware of the import of their conduct and any statements made during the development and conclusion of any partnering arrangement.

The concern of legal status of partnering agreement originated from the lack of certainty as to how will such relationship might be interpreted by the court, with the
consequence that it might resulted in a fundamental change in the way in which partners are required to treat each other.

**CONCLUSION**

The need for change within the construction industry is paramount to its survival. Those who fail to recognize and act within this scenario will struggle to succeed (Walker et al. 2002). So, partnering activities by public and private organizations today are starting to explore that territory and are demonstrating that change is possible. Partnering has proved successful in the United Kingdom, the United States, Hong Kong and Australia. The lessons learnt from those who have adopted it will aid local construction practitioners to minimize the risks brought by possible difficulties from implementing the concept of partnering; in which legal issues is one of them. This paper has discussed the legal issues that occur from this concept; the issues derived from the research will later be used to fulfil the ultimate objective of the study, to produce the guidelines of partnering contract which will serve as a suitable reference in the implementation of partnering in the Malaysian construction industry since there is no contract for partnering created yet.

**REFERENCES**


