How to value work scope omissions

While it might be expected that all variations to scope of works are treated the same way – whether it is an addition or an omission – there are different aspects to be considered when valuing omissions, says STUART JORDAN*.

WE have earlier looked at the practice of issuing instructions to omit works from the scope. The extreme end of de-scoping is the omission of all remaining works – effectively terminating the contract – in order to award those remaining works to another contractor.

This is still a rare event, and one which might fall foul of the law (depending on all the circumstances), but employers in the Gulf region seem to want to maintain the ability to order de-scoping (unlimited in degree and purpose) as an option in their contracts.

It is, therefore, worth considering how scope omissions should be valued. At first glance, this should be simple and uncontroversial: each element of the works will have been originally priced using a combination of unit rates and unit prices. If any parts are now not to be done, surely the contract allowances for them should simply be subtracted from the contract price? Like all construction lawyers, I am only an amateur quantity surveyor, but this looks like the obvious approach.

Well, it might not be that simple, for several reasons including:

- Because the instruction to omit an item might affect the way other works are carried out; and
- Because it might not be appropriate to value omissions in the same way as valuing additions to scope.

We can look at these two points together by considering what happens if the employer replaces a contractor work item with a better alternative which will accelerate works progress – or make it more cost efficient. Should the omission of that item be valued as a simple subtraction of the contract allowance (as described above) or should the efficiency be taken into account, so that the employer benefits from a greater reduction in contract price?

Jordan ... worth considering how scope omissions should be valued.

This question was one of several disputes which arose between the windfarm developer E.ON Climate and Renewables and its contractor MT Hojgaard. In this project, Hojgaard was contracted by E.ON to make and install monopiles for offshore wind turbines. The work was in delay and it was apparent that problems with the contractor's jack-up barge were at least part of the cause. E.ON issued three variation orders requiring Hojgaard to discontinue the use of that barge and to use another one, provided on a free-issue basis by E.ON. This brought about faster progress and the vast majority of the works were eventually completed using the new barge.

> **The court's most interesting point was about the approach to valuing omissions – stating this is different**

As a result of this, E.ON contended that valuation of the variation (specifically the omission of the original barge) should take into account the contractor's cost saving from the accelerated progress – that is, the contract price reduction should include a rate applicable to barge hire for the extended period it would have taken to complete the works using the original barge. Hojgaard, of course, argued for a valuation based on a barge hire rate just for the time it actually took to complete the works.

A separate issue was the applicable rates. The contract directed that variations (if not pre-agreed) should be valued in accordance with a schedule of rates specifically applicable to variations. Only if that schedule does not contain rates directly applicable to the variation, should suitable rates be created which reflect "the level of pricing" in that schedule. And if there are no applicable rates at all, there shall be a reasonable valuation. Note there is no reference here to the contract price breakdown.

This dispute came to the English Court of Appeal which agreed with Hojgaard. In relation to the acceleration question, the court noted that it was E.ON's decision to issue the variation when it could have let the delay run and levied liquidated damages instead. Once that variation was implemented, the reasons behind it should not be material in valuing it, and E.ON could not seek its remedy for the original delay through the variations mechanism.

The court's most interesting point was about the approach to valuing omissions – stating that this is fundamentally different to the valuation of additions because omission is the deduction of work which was originally priced in the contract, as opposed to valuation of additional work which was not in the original works scope. This necessitates considering the contract as a whole, including pricing risk. This meant considering the original contract price breakdown, and not just the schedule of prices for variations which E.ON had argued for.

This decision might surprise parties who have agreed a specific schedule to value variations and have given priority to that schedule in the rules for valuation. They might expect all varied works to be treated the same way – whether it is an addition or an omission – in accordance with that schedule. ■

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