

Can a Contractor Claim for Loss of Profit on Omitted Works?

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All standard forms of contract provide for the Architect or the Engineer to order variations to the Works, and such variations may include omissions.

Whenever variations are ordered that omit work, and particularly if such omissions are substantial in nature, contractors often argue that they should be entitled to claim the loss of the profit that they would have earned on such works. But is such a claim valid?

The answer is not clear cut, and depends, firstly upon whether the instruction omitting the works was a valid variation order, and secondly, if the variation is valid, upon what form of contract the instruction was given.

Invalid Variations

If the variation omitting works is invalid then such is a breach of contract entitling the contractor to damages, and it is clearly established that loss of profit can form part of such a claim for damages. But when is a variation omitting works invalid? Generally there are two such situations.

Firstly, where the works have been omitted and given to others to carry out it is clearly established that this is breach of contract and not a valid variation order. This point has been confirmed in a number of cases but was probably most succinctly put in the case of *Gallagher v. Hirsch* NY App Division 467 (1899) where the American court held that the word "omission" meant only work not to be done at all, not work to be taken from the contractor and given to another to do.

Secondly, where the power to order variations set out in the contract has been exceeded. For example in the Hong Kong Government conditions of contract variations must be either necessary or

desirable for the satisfactory completion or functioning of the works. Thus under such conditions works can not be omitted for example, to save time for completing the works, or to save the employer money.

Valid Variations

If, however the instruction omitting works is a valid variation order, then whether a contractor can claim loss of profit on such omitted works depends upon the wording of the conditions of contract. Looking at the two forms of contract most commonly used in Hong Kong:

The HKIA/RICS form of contract ("the Private Form") provides for the valuation of variations in Clause 11. Clause 11(4)(d) provides:

"The prices in the Contract Bills shall determine the valuation of items omitted; save that if omissions substantially vary the conditions under which any remaining items of works are carried out the provides for such remaining items shall be valued under rule (b) of this sub-clause."

This provision is not helpful to a claim for loss of profit, because it provides that the omitted works must be valued at the rate in the Contract Bill, i.e. omitting the full value, including profit, of the item in the Contract Bills. Nor is the proviso of any assistance in such a claim because the variation must substantially vary the conditions under which the remaining items are carried out before the remaining items can be re-valued. Loss of profit on an omitted item will not in itself vary the conditions in which the remaining items are carried out. So the proviso does not appear applicable in this situation.

However, Clause 11(6) provides the Contractor with an entitlement to claim 'direct loss and/or expense' incurred by reason of a variation.

In the case of *Wraight Ltd v. P H and T Holdings* (1968), a contractor's contract was wrongly determined with the work part completed. The determinations clause provided for the contractor to be paid

"Any direct loss and/or damage caused to the contractor by the determination."

It was held by the court that this wording included loss of gross profit on the uncompleted work. Therefore, following the *Wraight* case it would appear arguable that a claim for loss of profit on works omitted by way of a variation can be claimed as direct loss and or expense under Clause 11(6) of the Private Form.

The Hong Kong Government conditions of contract ("the Government GCC") provide for the valuation of variations in GCC Clause 61. Sub-clause (1)(a) of that clause provides that:

"Any item of work omitted shall be valued at the rate set out in the Contract for such work."

This is similar to the first part of Clause 11(4)(d) of the Private Form and in itself is not helpful to a claim for loss of profit, because it provides that the omitted works must be valued at the rate in the Contract, i.e. omitting the full value, including profit, of the item in the Contract.

A similar proviso to that in Clause 11(4)(d) of the Private Form is also contained in GCC Clause 61, and provides for re-rating other item or items in the Bills of Quantities if a variation renders such rates inapplicable or unreasonable. However it is again not considered possible to argue that this power extends to re-rate other items in the Bills of

Quantities on the basis that there has been a loss of profit on works omitted.

So are there any other clauses in the Government GCC that would permit a claim for loss of profit on omitted works? The Government GCC equivalent to Clause 11(6) in the Private Form is GCC Clause 63. GCC Clause 63 like Clause 11(6) provides for the reimbursement of expenditure consequential from a variation order. However GCC Clause 63 is different in two important aspects.

Firstly the clause gives an entitlement to costs (defined as expenditure actually incurred) rather than direct loss and expense. From a loss of profit point of view this is not necessarily fatal because it is possible to argue that the word expenditure should be given its dictionary definition which includes 'a sacrifice', i.e. a loss and in particular a loss of profit.

Secondly however, GCC Clause 63 is different to Clause 11(6) of the Private Form because it only gives entitlement to reimbursement of such costs where the variation has caused a disturbance to the progress of the works. A variation omitting works would not normally cause a disturbance to progress.

In conclusion therefore, whilst a claim for loss of profit will always be successful where the works were omitted by way of an invalid variation order, where the variation is valid it seems clear that the Government GCC does not provide a means for a contractor to claim for loss of profit on works omitted. Under the Private Form however such a claim is possible as a direct loss and expense claim under Clause 11(6) and on the basis of the decision in the *Wraight* case.

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