Contractual Strategies For Building Maintenance

Both public and private sector owners are increasingly considering the benefits of implementing long term management and maintenance strategies to manage and maintain their plant and facilities. In economic terms, owners consider that this is an efficient way of doing so which, over time, results in decreases in operational and maintenance costs.

The recognition of the importance of the management and maintenance of plant and facilities has, in turn, led to an increase in contracting out of these functions.

Given the increase in outsourcing of maintenance services what contract strategies are available? There is presently no standard form of general conditions of contract for the maintenance of plant and facilities. The general conditions of standard form construction contracts (such as AS2124-1992 and JCC-C and JCC-D) are not appropriate, as different considerations are involved. More often than not construction contracts involve (or ideally should involve) a well-defined scope of work which a contractor must perform for a lump sum.

A maintenance contract on the other hand will generally not be capable of defining the scope of work with as much certainty as a construction contract. Although maintenance contracts will include planned or routine preventative maintenance tasks (which can be priced by way of fixed price), they will also need to cover unforeseen problems such as attending to breakdowns of plant or equipment.

In view of the greater uncertainty as to the scope of work under a maintenance contract, one tends to find a greater range of payment mechanisms in such contracts. Broadly speaking, maintenance contracts tend to provide for payment in one (or a combination) of the following ways:

- lump sum;
- schedule of rates;
- management fee plus costs;
- target cost with incentives.

The appropriate pricing mechanism depends upon each particular owner's requirements. For example, one innovation in building maintenance contracts is the use of contracts tying contractor revenue to performance. This mechanism can be applied to almost any of the above pricing structures.

Lump Sums

Like any lump sum contract, a lump sum maintenance contract requires the scope of work to be defined with certainty. This can vary from contracts which prescribe when each item of plant and equipment is to have maintenance work performed upon it, to contracts which are performance based and therefore only specify the standards which must be achieved. The latter will require the contractor to perform all routine and unforeseen or breakdown maintenance tasks and to supply all labour, materials and spare parts for this purpose. There will also be an obligation to ensure that the facilities which are being maintained achieve the performance measures and targets set out in the contract. Failure to ensure that these facilities achieve these standards will result in penalties or liquidated damages being deducted from the lump sum.

In any performance based contract (whether for a lump sum or otherwise) the owner will need to carefully develop the operating standards which the contractor will need to achieve. Not only will these need to be exhaustively and clearly expressed, they also should be practical, achievable and measurable. Performance based contracts (particularly if for a lump sum) may result in a contractor performing the minimum work it needs to in order to achieve the required standards. This may result in long term problems which only manifest themselves after the contractor's term has expired. This risk can be managed by:

- setting a base amount of work which the contractor must perform;
- monitoring the contractor's performance by, for example, requiring reports after each preventative maintenance task or requiring random audit reports from an independent contractor from time to time;
- considering long term arrangements with contractors so as to minimise the risk of a contractor "under-maintaining" facilities so as to maximise profit; and
- providing for penalties, if after the end of the contract, problems arise which can be attributed to the contractor's failure to adequately maintain the facilities during its term.

Obviously, this is a matter that needs to be carefully thought through by any owner deciding to engage a contractor on a performance based maintenance contract.

Schedule of Rates

A schedule of rates maintenance contract will provide the least certainty as to final cost. It will specify numerous rates which the contractor will be paid for performing work and supplying labour, materials and spare parts.

A schedule of rates is more likely to be used to cover work not covered by a lump sum or as a means of determining cost in a cost plus fee arrangement.

Management Fee Plus Cost

This is essentially a cost plus arrangement under which the contractor will be paid a fixed fee plus its "costs".

"Costs" will be defined by a schedule, usually in the form of a schedule of rates. This will enable the owner to have the rates used in determining "costs" competitively bid. The contractor is essentially being engaged by an owner to manage the process of maintaining its facilities.

This is a system that is becoming popular with owners of large sites or of a number of facilities. The attraction for such owners is that by combining a number of buildings or facilities in a geographical area they can achieve greater economies of scale (through a combination of increased turnover and the tender process) by letting the maintenance of all these buildings to one maintenance management contractor. Such contracts often cover a number of buildings on a very large site (e.g. universities, hospitals or Defence bases). In view of this it is often not possible to define the scope of work in a manner which will enable the owner to let the work on a lump sum basis.

Target Cost With Incentives

The concept of a target cost with incentives can be employed with either of the previous two pricing mechanisms. Usually the target price is not guaranteed (as opposed to a lump sum). Rather, it is used as a benchmark from which to determine whether a contractor has earned its incentive. For example, an owner could enter into a maintenance contract under which:

- the annual target cost was the previous year's actual recorded maintenance cost of the relevant facilities;
- the parties agreed to the performance standards which were to be achieved;
- the contractor was paid a fee plus costs (using a schedule of rates) for work performed; and
- if the amount of the fee and costs were lower than the target cost the parties would share the saving in an agreed manner.

An incentive based contract is intended to create an environment in which the interests of the owner and contractor coincide (unlike a lump sum) in that it is in the interests of both to minimise maintenance costs. As, however, the contract is not a lump sum contract, the owner retains control and can direct the contractor to perform as much (or as little) work as it requires. Reserving this power will make it difficult to require the contractor to share any cost overruns (as opposed to savings). It will, however, overcome the risk of the contractor "under-maintaining" the facilities to minimise cost and therefore increase savings (and decrease the risk of long-term problems with the facilities).

Conclusion

These are some considerations to bear in mind when outsourcing maintenance services. As the opportunities in this area increase new and innovative ways to contract out maintenance sources will no doubt develop.

In all cases, however, owners should tailor the contract to their requirements. The standard form construction contracts are inappropriate.

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