

Virtus

The Virtus Fitting Out Guide

Property Old & New

Broadly the property market consists of three major sets of players:

- Developers and Financial Institutions
- Design and Construction Teams
- Building Users

The over simplified split of the industry describes what has, during the last decade, evolved into an extremely complex blur of overlapping roles and competitive invasion across traditional professional and skills boundaries.

Key Players in the Property Industry

The Funders and Developers

There are two main sources of property funding in the UK – the Banks and the Financial Institutions.

Working closely with both funding institutions and developers are the Property Agents, who provide a professional link between funders and developers as building suppliers, and the marketplace of potential building occupiers.

In order to protect the long term value of their property investments over time, various funding institutions have exerted considerable pressure on the characteristics of a new building or redevelopment. Currently the property market is questioning whether the brief that the funding institutions effectively dictate is relevant. Many people argue that the modern building today is over specified.

The typical criteria that a design and construction team will be expected to meet today are:

- 10m² per person
- large floor plate sizes
- generous slab to slab heights (3.85m to 4.2m), floor to floor heights of between 2.65m and 2.75m.
- floor loadings up to 5Kn/m²
- full VAV air-conditioning
- raised floors
- suspended ceiling
- small power provision of 30-40 watts/m²



The End User

Whilst funding institutions may exert considerable pressure on the specification of a construction project the influence of a potential end user is never ignored. Particularly so when he is either prepared to commit to a particular building early in the project cycle, or indeed, he is either partial or total funder of a project. As a potential leaseholder for a speculative development the development team will be looking to provide as many of the incoming tenant's specific requirements as possible without tailoring the building so that it becomes unusable by another organisation.

Broadly, if an end user is committed to a move there are two choices: move to a new or refurbished building. Each have their respective advantages and disadvantages.

New Build, the Key Issues

Moving to a new building allows an organisation to match their own requirements to a potential new building. During the last few years the property market has become very aware of the need to allow an incoming tenant as much choice as possible in tailoring a building to meet his own need. As a result, many new developments offer an incoming tenant the choice of either taking on a building finished to 'developers specification' or 'shell and core'.

- Developers standard fit out usually offers the incoming tenant a pre-defined package of services and finishes that typically includes a raised floor, a floor finish such as carpet tiles, suspended ceilings, air-conditioning and light fittings.
- Shell and core provides a basic building shell that typically includes staircases, lifts, toilets, central HVAC plant and ducting. The tenant is then offered a financial contribution to fit the building out to his own specification.

Refurbishment, the Key Issues

Refurbishment of either existing premises or choosing an older building to move to, throws up a different set of considerations:

- Structural condition of the building. What work will be necessary to return the building to a solid state of repair?
- Adaptability. Older buildings can prove difficult to adapt to meet the needs of modern business. Floor to floor heights may limit services distribution choices. Quality of space may limit the type or quality of space that an organisation may require to achieve operational efficiency. Can appropriate support facilities, for example catering, be provided? Would building security be an issue?
- Running and maintenance costs. Will they be affordable and reasonable?

The Occupier's Brief

To make an informed choice it is vital that the end user has a clear set of criteria against which he can measure property options regardless of refurbishment or new building choices.

Some of the key criteria to consider are:

- Building size.
- Programme – key deadline dates for occupation. Key types of space – offices, support spaces, manufacturing etc.
- Quality of building.
- Building services – heating, lighting, ventilation, cooling – dependent upon the way the building will be occupied.
- Quality of working environment – finishes and any maintenance criteria.
- Configuration of space – dependent on working style of organisation – a major consideration is the mix of open and enclosed space.
- Anticipated change. How stable is the organisation – is growth predicted, or are changing work patterns going to limit expansion?

The Design and Construction Team

Traditionally there was a relatively clear split between 'design and production' and 'construction'. The professional consultant team, headed by the Project Architect, comprised the former, and the construction team comprised the latter. The Project Architect tended to retain power throughout a project. Because procurement routes have changed so fundamentally during the last few years relationships and responsibilities in the design and construction team have been re-arranged and different contract choices will attribute different degrees of risk and responsibility to the team members.

However, whatever the contract choice most major project teams will comprise:

- Project Manager (independent or one of the other key team players)
- Project Architect or Designer
- Quantity Surveyor
- Structural Engineer
- Services Engineers
- Specialist professions (e.g. IT specialist)
- Main and sub-contractors

Procurement

Contractual relationships are powerful mechanisms for defining responsibilities and working relationships on a construction project. For many years the professions, led by the architect, effectively controlled contract choice. The professional institutions defined the services offered by their members and set mandatory fee scales. The invariably used contract was the JCT Standard Form of Contract (although 11 'Standard Forms' are produced). During the construction frenzy of the late 1980s it became an increasingly unsatisfactory contract for clients and caused considerable frustration to the contractors.

Today there is a greater willingness to more closely consider the benefits and penalties of one procurement choice over another:

Contract Choices

The Traditional Contract

A Project Architect leads the professional design team, which usually includes a Quantity Surveyor and Structural and Services Engineers. The final design solution is resolved to the last detail, competitive tendering to appoint a contractor then follows. As price is a key choice criteria the contractor submits his lowest price, and if necessary, negotiates aggressively to make up profit later by negotiating additional payments for increases or changes to scope of works. The professional team is unable to use the contractor's construction skills to test buildability. On complex projects the underlying adversarial nature of this procurement route can make it costly and difficult to manage to the client's best benefit.

The traditional project programme tends to be slow. Slow because project execution is linear, all design is finally resolved before tendering. Only then can site operations start, the contract does not allow for project phases to overlap.

Up until the end of the latest construction boom traditional contract relationships still accounted for 65% of the construction work undertaken, it is now a constantly declining percentage and it is a less likely procurement choice on a major project today.

The Management Contract

A Management Contractor is drawn into the professional team early in the project. He is paid a fee to manage the construction process, and in the early project phases advises on buildability. By dividing the work into 'packages' the project is broken down into phases with different start dates. Construction can commence on individual packages of early work before later packages are designed or tendered. All construction work is let through competitive tendering in subcontractor packages by the Management Contractor.

The contract requires a strong client, who benefits from flexibility, but must be prepared to work with an unknown final project cost until the project is well underway. No one member in the delivery team has been delegated ultimate responsibility; the client needs to stay close to his project.

Until recently Management Contracting accounted for approximately 12% of contracts.



Construction Management

During the late 1980s and early 1990s Construction Management became a popular procurement route on major construction projects. The principal uniqueness is that the construction manager is now a direct consultant to the client with his role very clearly being focused towards representing the client's priorities. The client will sign contracts directly with all works contractors; his own management skill must therefore be considerable, but it is now easier for him to identify specific poor contract performance and seek compensation accordingly. Construction managers tend to take on many of the Quantity Surveyor's responsibilities.

Architects are clearly directed towards conceptual design to the extent that specialist works contractors may take responsibility for their own detail design.

This method most closely resembles the typical German and French procurement choice and it is therefore interesting that it has gained popularity in the UK as EC harmonisation approaches.

Design and Build

A contractor bids a fixed price for a project based on a client's specification. The contractor, who earns his profit from an efficient delivery, is responsible for design and execution of the total project. Design quality and fees are defined by the contractor. As the project is won competitively the contractor is often expected to work on a speculative basis – either drawing up a client's brief with the hope that he will be appointed, or on a 'no win, no fee' basis. It is an appealing procurement route for a client who has a simple project. Relationships are clear and price is guaranteed. In 1985 design and build contracts totalled 10-12% of all contracts, by the end of the decade it was 20% and it is forecast to increase by 1% per annum for the next decade.



Summary benefits and compromises according to different contract choice:

Contract	Potential Benefits	Possible Compromise
Traditional	Price – is not fixed until all design decisions taken, less chance of major unknown costs. Quality – very clearly defined requirements before contractor tenders.	Time - nothing is started in advance of final detail design decisions being agreed.
Management	Time – project is divided into packages which can be programmed to start in isolation of other design decisions being fixed. Quality – each package of work can be clearly defined in terms of required quality.	Price – because major chunks of the project may not be tendered until late in the construction process final contract price is unknown until the project is considerably advanced.
Design and Build	Price – fixed very early in the project, unlikely to change. Time – completion date agreed, penalties if not met.	Quality – as all financial and programme risk has been placed with contractor the client has less control over project quality

Project Management

Key to the successful delivery of any project are project management skills. During the last few years the role of the independent Project Manager within the design and construction team has firmly taken root.

Project Management may be defined as the overall planning, control and co-ordination of a project from inception to completion. Successful project management meets Client's requirements by delivering a project on time, within authorised cost and to the required specification and quality standards.

Very simply the Project Manager is the Client's representative communicating decisions to the project team, ensuring their implementation, monitoring progress and reporting back.

The role of a Project Manager clearly demands a person with considerable understanding of technology, the process of building, design requirements and the complex inter-relationships of law, finance and human relationships. A Project Manager has to develop and maintain a strong team spirit within the disciplines of the project; the ability to organise and lead is paramount.

The Project Manager, acting on behalf of and representing the Client, has a duty to provide a cost effective and independent service integrating and managing different disciplines and expertise and to satisfy the objectives and provisions of the project brief from inception to completion. The services provided must be to the Client's satisfaction, safeguard his interests at all times, and where possible, give consideration to society and the environment.

Project Management reinforces Client control over the complexities of modern development. By employing a professional and appropriately experienced Project Manager the Client will gain significant advantages in increased efficiency, economy and communication.

As early as the feasibility stage the Project Manager will identify the professional resources needed at each stage of the development and minimise expenditure on abortive work. Once the development is underway he will control his Client's financial commitment, ensure compliance at all times with the brief (which may change to suit the Client's evolving requirements) and secure the optimum performance from the project team.

The Project Manager must meet a Client's need for positive control over time, cost, quality and function.

Cost Management

For many clients the most important measure of project success is whether a project is completed within the agreed budget.

Cost budgeting and monitoring has traditionally been undertaken by a Quantity Surveyor. Today cost control responsibilities, depending on contract choices and client preferences, may fall to different members of the professional team. As a project develops and progresses to and through the construction stage, suitable financial management procedures and documents must be established to facilitate good financial administration to protect the client's interests:



Budget estimates should be prepared at the earliest possible stage of the development. These initial estimates, and all future costings will be based on the client's requirements, using extensive local knowledge and cost databases built up over many years.

A Cost Plan establishes a cost limit for the project. A detailed cost plan is then prepared. This Cost Plan will be divided into separate buildings (if appropriate) and elements such as foundations, structural frame, mechanical and electrical services and finishes will form the basis for ongoing cost management.

Subsequent development of the design of each element will be carefully monitored against the cost plan to ensure the design remains cost effective. During this process a good financial controller will seek economies that can be implemented to improve the value of the project. Value engineering studies will be carried out to ensure real value for money is being achieved.

Running costs and life cycle costs, contractual issues and tax considerations should be evaluated.

Bid documents should be prepared for competitive tendering purposes or for negotiated tenders as appropriate.

Tenders received will be examined in detail, recommendations made as to the most suitable contractor and formal contract documents prepared.

During construction the financial implications of proposed variations to the works, and other instructions having a cost effect, will be continually monitored. Corrective measures should be taken to keep the overall costs within approved limits.

Regular Financial Reports will be prepared and issued regularly to show the effect of all cost adjustments arising during construction.

Cash flow forecasts will be established based on the construction programme. Actual expenditure will be monitored against forecast expenditure.

Stage payments to the contractor will be assessed. Valuations will be prepared recommending the amounts to be certified based on the progress of the works. At project completion a detailed final statement of account will be prepared showing the final cost of the project.

The active cost management service and regular liaison with the design team will bring added value to all stages of the project from inception to completion.

Acquiring and Disposing of Property in the UK

This section identifies the most likely legal issues which may arise on the acquisition, disposal or development of property and suggests when it may be advisable to seek expert advice from solicitors and surveyors.

General Issues Relating to Property in the UK

Legal title to property

There are two types of legal title to property:

- Freehold – a freehold interest in land is not limited in time and is freely transferable by the owner. It is, in effect, owned absolutely by the holder and is not capable of being overridden by a superior claim.
- Leasehold – a leasehold is one where the right to the use of the property is limited in time and will be subject to various restrictions. A 'leasehold' is a legal right to exclusive possession of land or building or part of it described in a lease, for a specified period of time and usually for a payment of monetary rent. A lease will impose obligations on both Landlord and Tenant and apply to them both throughout the terms of the lease.
- The obligations of a Landlord and Tenant will vary from lease to lease, and the law does not require that standard lease terms be accepted. Lease terms are settled after negotiation between the parties. From a Tenant's point of view it will be important to consider what type of ownership is required, bearing in mind the requirements of its business.

Planning Issues, Local Authority Searches etc.

Before acquiring an interest in land, it is most important to check that the property can be used for the purpose for which it is required, and that there are no existing restrictions or proposals which will prevent such proposed use. This information is obtained by searching various Registers maintained by the Local Authority in whose area the property is located. If the existing permitted use of the property does not match your requirements you can consider applying for planning consent for your proposed use. You should then weigh up the likelihood of achieving a successful application. It is therefore important not to commit to a building until the planning issues have been resolved.

Environmental Questions

A purchaser of a freehold interest in land (or a leaseholder taking on responsibility for the land) should consider UK environmental legal requirements (e.g. by production to toxic waste etc.)

- Will the business or activity to be undertaken on the land itself infringe environmental requirements (e.g. by production to toxic waste etc.)?
- Is the land contaminated or causing contamination to adjoining land? (It will be important when purchasing land to investigate the past, because there can be significant liabilities for "clean-up" costs for the unwary).
- If there is any concern, a purchaser should consider arranging for an Environmental Audit to be carried out.



Condition of the Building

If you are purchasing the freehold or taking a leasehold interest which carried with it an obligation to keep the building in good repair or contribute towards the cost of carrying out that work, you should ensure that the building is in the required state of repair and condition. An independent surveyor will be the expert to approach for a Structural Survey. If it subsequently turns out that the opinion of the surveyor was wrong it may be possible to sue him for negligence in giving a careless assessment of the standard of repair of the building.

Disposing of Property

In view of the possible need in the future to dispose of the property you should ensure that there are no unusual or unacceptable restrictions on your freedom of action. A freehold property should have no such restrictions. With a leasehold property, however, it is usual that the landlord would require to approve any proposed transfer of the lease or the creation of any subsidiary interest. Therefore, you should include in the terms of the lease the right to assign the leasehold interest or sub-let the whole and (if appropriate) any reasonable severable part of the property (usually with the Landlord's consent which should not be unreasonably withheld). You should also ensure that group companies can occupy the property without the need to obtain the Landlord's consent.

Leasehold Property

The terms of every lease can be subject to negotiation.

A Tenant should normally expect to be required to:

- Keep the property in good repair
- Pay for the cost of insurance, local taxes and other outgoings

A lease will usually also:

- Regulate how the Tenant may use the property
- Control the carrying out of alterations
- Ensure that the Tenant does not cause any nuisance during his occupation
- Limit the Tenant's ability to dispose of the property

There are a number of major points to bear in mind when considering a proposed leasehold interest:

- Length of term – until recently, leases on substantial premises would have been for 25 years. Today Landlords may be willing to agree to grant a lease for shorter period (e.g. 10 years) or agree to break clauses in a long lease enabling the lease to be ended at a specified time (e.g. at the end of each 10th year).
- Rent Reviews – a lease of more than 5 years will typically entitle the Landlord to request that the rent is reviewed at the end of each fifth year of the term. The Tenant must be clear as to the implications of the rent review provisions, and ensure that clause details are carefully drafted to avoid unexpected results in later years.

Insurance Arrangements

Landlords usually prefer to retain responsibility for the insurance of the building, even though the Tenant pays the premiums. You will need to ensure that an adequate range of risks is covered by the insurance policy and that the Landlord gives an express covenant to reinstate the premises should an insured risk occur causing destruction. It will also be vital to ensure that the insurance company cannot recover from you as Tenant by way of subrogation the amount which it, as insurer, has paid out to the Landlord as the insured party. As Tenant you will be responsible for insuring your own contents in the property.

Security of Tenure

UK law provides a Tenant occupying premises for the purposes of its business with a considerable degree of protection against being removed from those premises at the end of the contractual term. Generally a Tenant occupying premises at the end of a lease and continuing in business has the right to a new lease essentially on the same terms (except for the rent which will be increased to the current market rent) unless the Landlord can prove one of a limited number of grounds to oppose the Tenant's claim. However, a Tenant must comply strictly with time limits for service of notices and the making of appropriate applications to the Court in order to protect his right to a new lease. It is the Landlord and the Tenant who agree this protection and it may be waived by making a joint application to the Court.

Privity of Contract

As the law stands, a Tenant is not released from its obligations under the Lease (including the obligation to pay rent) when it disposes of its interest in the property. The UK Government has recently announced that it intends to review and probably reform this area of the law. It is anticipated that the reforms will provide for an original Tenant to cease to be liable to the Landlord after its assignee has itself disposed of the property. However, these reforms are not expected to be retrospective, so a Tenant should try to negotiate a release of such obligations.

Building or Refurbishing Premises

A party wishing to build or refurbish premises can either engage a developer to carry on the development on his behalf, or act as 'the Employer' by appointing appropriate contractors and consultants himself.

Engaging a Developer

The Client may enter into an agreement with a developer to build or refurbish the property which, once complete, would be purchased by the Client. The development agreement between the Client and the Developer should clearly make the Developer responsible for carrying out the development but allow the client certain rights to be involved in the design and construction process. Consequently careful consideration should be given to the drafting of the development agreement.

Acting as the Client

If the Client wishes to procure the construction works on its own behalf, the traditional approach is for the Client to engage a professional team (including architect, structural, mechanical and electrical engineers, quantity surveyor and, perhaps, a project manager) under direct contracts of appointment between the Client and the relevant consultant.

Consultants favour the standard form of appointments produced by their respective professional organisations although these documents, not surprisingly, are concerned more with protecting the Consultant than the Client and the Client should always consider appropriate amendments to these forms, or preferably, use a form of appointment specifically prepared for a particular project. Consultants may be remunerated in different ways:

- a fixed price
- a percentage of construction costs
- a time charge basis

The level and basis of the fee is subject to negotiation.

Under the traditional structure in the UK, the Client would also employ a Contractor to carry out the construction works (with design being carried out by the appropriate consultants). The Contractor may sub-contract a significant proportion (if not all) of the work although he would remain responsible for the acts of his Sub-contractors.

The forms of construction contract between the Client and the Contractor generally used in the UK are detailed and comparatively complex documents which set out both the legal rights and obligations of the parties and the practical mechanisms for the carrying out of the Works. Many standard form construction contracts have been produced by organisations such as JCT and ICE but these forms have been the subject of much criticism and are frequently amended for a particular project. Construction contracts and related contractual documents (such as bonds, warranties, guarantees and technical documents) should be drafted with great care.

Alternative Contractual Structures

In recent years, alternatives to the traditional main contractor approach have arisen. These alternative approaches include design and build (where the Contractor is responsible for both the design and the construction of the works). At the other end of the spectrum are management contracting and construction management in which the main contractor's role is restricted to that of a manager co-ordinating the work of various specialist trade contractors who are each responsible for their own work.

Risk and Responsibility

The construction process involves considerable risk. Different contractual structures distribute risk between the various parties differently. Accordingly, great care must be taken in choosing and negotiating construction contracts to ensure that risk and responsibility are allocated appropriately.

Construction Contracts

Construction contracts should adequately deal with such issues as:

- The appropriate standard of care to apply to the contractors and consultants
- The required performance
- Security
- Insurance
- Delay and liquidated damages
- Changes to the Works.
- Payment

The contract should also be tailored to suit the requirements of the particular project so that it can be used as a tool to assist in the construction process as well as defining the parties' obligations and responsibilities.

Conclusion

Building, moving or refurbishing premises is one of the most expensive decisions that a company undertakes. Potentially it is also one of the most disruptive exercises and can distract an organisation for a long period. A Facilities Manager can draw upon a wide array of professional advisors to support him during this period. He can also protect his company's best interests by establishing contractual relationships that deliver his requirements. Above all he should have a clear set of objectives he wishes to achieve, strong managerial skills and the support of his senior colleagues to ensure that he meets his deadlines and achieves the quality and value he wants.

Virtus

Virtus Contracts Ltd

tel: 020 7234 8600 | fax: 020 7234 8601 | email: info@virtus-contracts.co.uk | web: www.virtus-contracts.co.uk