# Report
# A Review of the Concepts and Definitions of the Various Forms of Relational Contracting

## Research Project No: 2002-022-A-01


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Value in Project Delivery Systems: Facilitating a Change in Culture


Leaders in Construction and Property Research

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# Preface

Partnering, alliancing and relational contracting have been the subject of many studies over the past 15 years in many countries. This document aims to identify and to present a series of definitions based on the major studies undertaken in this area. The reason for this is that the culture project, Value in Project Delivery Systems: Facilitating a Change in Culture, needs to establish a working definition for alliancing and partnering to be used during the study. It should be noted that the documents referred to here are not those used by Main Roads and Public Works Departments. However, the authors are cognisant of the documents produced by Main Roads and Public Works do have their own working definitions. Hence, it is intended that all members of the project team can review the Queensland definitions and the more global definitions presented in this document before drawing a conclusion as to which specific definition is most useful for the research being conducted. It may well be that Main Roads and Public Works maintain their own separate and distinct definitions but, as long as all team members are aware of the working definitions and the range of definitions worldwide, this will not have any detrimental effect on the progress of the project. The document presented here provides a state of-the-art review of the definitions and concepts in this area and is intended as a discussion document and not as a definitive report on the definitions of alliancing, partnering and relational contracting to be adopted.

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# Executive Summary

Partnering is defined as a structured management approach to facilitate team working across contractual boundaries. Partnering is primarily concerned with "maximising effectiveness" and partnering has three essential components:

- establishment of agreed and understood mutual objectives;
- a methodology for quick and cooperative problem resolution;
- a culture of continuous, measured improvement

It is these elements that QDMR and QDPW wish to see incorporated into their projects.

Partnering has been discussed by many commentators and categorised as project partnering and strategic partnering Project partnering is partnering undertaken on a single project. At the end of the project, the partnering relationship is terminated and another relationship is commenced on the next project. Project partnering was pioneered in the USA construction industry during the mid to late 1980s. Strategic partnering takes place when two or more firms use partnering on a long-term basis to undertake more than one construction project, or some continuing construction activity (RCF 1995).

Green (1999) offers a counter view on partnering. Green (1999) has pointed out that the propagation of partnering in construction is to exercise increased control over the construction supply chain. However, another, alternative view is that trust-based partnering encourages parties to adopt higher ethical standards.

Strategic alliances enable organizations to speed up the market-entry process and increase their responsiveness to consumer markets (Howarth et al., 1995). A project alliance (strategic alliance) is a business strategy where sponsor and commercial participants' objectives (client's objectives) are aligned to:

- Maximise performance;
- Reduce cost; and
- Achieve outstanding results in the sponsor's key project objective.

Like partnering and relational contracting, trust between strategic alliance partners is important because it creates an opportunity and willingness for further alignment, reduces the need for partners to continually monitor one another's behaviour, reduces the need for formal controls, and reduces the tensions created by short-term inequities. Hamel (1989) suggests that organizations that enter into collaborative alliances (short-term) are aware that their partners are capable of disarming them. Parties to these alliances have clear objectives and understand that their partner's objectives will affect their success. Cooperative alliances (long-term) encourage alliance partners to commit their resources to the relationship to generate mutual learning (Love et al., 1999). Ketelholm (1993) suggests that cooperative strategic alliances can create a competitive advantage.

Relational contracting embraces and underpins various approaches, such as partnering, alliancing, joint venturing, and other collaborative working arrangements and better risk sharing mechanisms. Relational contracts are usually long-term, develop and change over time, and involve substantial relations between the parties. The characteristics of relational contracts and construction contracts are summarized in the report.

Various authors have suggested that a relational approach to contractual governance entails long-term social exchange between parties, mutual trust, interpersonal attachment, commitment to specific partners, altruism and cooperative problem solving. It has been suggested that construction contracts are typical relational contracts as construction contracts often involve numerous parties and subcontracts with heavy informational exchange in the construction activities. Relational contracting provides the means to achieve sustainable, ongoing relations in long and complex contracts by adjustment processes of a more thoroughly transaction-specific, ongoing, administrative kind.

Thus, it can be argued that more relational and performance oriented contractor selection would encourage an amicable relational contracting environment and more collaborative teamwork. Relational contracting approaches are expected to work in almost any environment if applied properly.

# Introduction

Partnering has been defined in many ways. It can be considered as an individual project mechanism or can be considered as a long term strategy. Alliancing is normally assumed to be a long term business strategy linking together client, contractor and supply chain. Relational contracting goes further than this and brings in the whole philosophy of the value chain and the linking of the interdependent parts within the construction project as a key business objective. This document aims to review existing definitions of these three concepts and present and overview of the current state of-the-art in terms of their use and implementation. The document should be useful for all of those project team members looking to sharpen their understanding of the various concepts and will also provide a platform for debating the current state of the definitions and implementations being used in Main Roads and Public Works Departments.

# Definitions

Many definitions and ways of looking at partnering and alliancing are shown below. However, in order to set the scene, the researchers have developed their own definitions of how, in general, QDMR and QDPW view traditional, partnering and alliancing.

Traditional contracts operate under ***AS2124*** or similar, and are adversarial in nature, the contractors have being selected mainly on the basis of lowest price in a competitive bid and the superintendents see their role as gatekeepers, safeguarding the client's interest.

Partnering has been implemented by putting a partnering agreement on top of the traditional contract and encouraging contractor, consultant and client to proactively address project risks, identify them before they affect the project and take action, jointly agreed to manage the risk. The problem with this approach is that superintendents have continued to see their role as gatekeepers rather than as team members and contractors have kept one eye on the conditions of contract and claims, whilst going through the partnering process.

Alliancing has been implemented, in the main, through a management or cost plus contract where pain and gain are shared between the parties to the contract and a team approach is engendered in many instances by locating all team members in the same office. Thus, the traditional, adversarial roles have been removed by adopting a different form of contract and way of working out issues, particularly in the area of RFIs.

## Partnering

Partnering is defined as a structured management approach to facilitate team working across contractual boundaries. Its fundamental components include mutual objectives, agreed problem resolution methods, and an active search for continuous measurable improvements (CBP 1998). Construction Industry Institute Australia (1996) suggests a partnering charter is developed to run in parallel with a traditional construction contract to provide guidelines to the relationship between the organisations. CII defines partnering into three types, namely experimental partnering, packaged partnering and committed partnering, as illustrated in the figure below.

| Type | Description | Outcome |
|---|---|---|
| Experimental partnering | • Charter, workshop, small number of follow-up meetings<br>• Usually first partnering experience<br>• Minimally resourced<br>• Often seen as a 'toe-in-the-water' exercise | • Often unsuccessful, generally because of lack of clear understanding, commitment and structure |
| Packaged partnering | • Offered as part of a contractor's tender or imposed upon the contractor after the tender is accepted<br>• Often involves only the client and contractor<br>• This model is usued very successfully as a marketing tool | • Problems may arise from lack of commitment and understanding of each stakeholder's objective perceived to be cooperative at the outside of a project may not necessarily last for the duration of the contract |
| Committed partnering | • Often developed as a result of first, unsuccessful experience<br>• Incorporates as many stakeholders as possible in a tight, well facilitated dispute resolution mechanism<br>• Well resourced | • Problems may arise from lack of commitment and understanding of each stakeholder's objective<br>• A client-contractor relationship perceived to be cooperative at the outside of a project may not necessarily last for the duration of the contract |

*Fig. 1: Australian Partnering Firms (adapted from CII 1996 by Walker & Hampson 2003 – p. 48)*

Partnering is also recognized as a method of improving communication mechanisms and technologies, responding to innovative construction projects, creating a less stressful working environment and reducing transaction costs resulting from uncertainty, competition and information asymmetry (ECI 1997; Liu & Fellows 2001). One of the most commonly used definitions for partnering was written by CII as follows (CII1991):

"…a long-term commitment between two or more organizations for the purpose of achieving specific business objectives by maximizing the effectiveness of each participant's resources. This requires changing traditional relationships to a shared culture without regard to organizational boundaries. The relationship is based on trust, dedication to common goals, and an understanding of each other's individual expectations and values."

Weston & Gibson (1993) find the three elements in the definition given by CII are trust, shared vision and long-term commitments. Peters et al. (2001) suggest partnering relies solely on the commitment of individuals due to the fact that partnering charter is not legally binding. Green (1999) sees partnering as primarily concerned with "maximising effectiveness". The definition given by Bennett and Jayes (1995) reflects similar themes:

"…partnering is a management approach used by two or more organizations to achieve specific business objectives by maximizing the effectiveness of each participant's resources. The approach is based mutual objectives, an agreed method of problem resolution, and an active search for continuous measurable improvements."

It is noticed that improvement must not only be continuous but measurable as well. The definition offered by "Egan Report" provides a similar tone (DETR, 1998):

"…partnering involves two or more organizations working together to improve performance through agreeing mutual objectives, devising a way for resolving disputes and committing themselves to continuous improvement, measuring progress and sharing the gains."

The DETR further consider partnering to be a "tool to tackle fragmentation" which is increasingly used by the best firms in place of traditional contract-based procurement and project management (Green 1999). According to the Construction Industry Board (1997), partnering has three essential components:

- establishment of agreed and understood mutual objectives
- methodology for quick and cooperative problem resolution
- culture of continuous, measured improvement

Partnering has also been discussed by many commentators and categorised as project partnering and strategic partnering (Gaede 1995; RCF 1995; Matthews 1996; Matthews & Rowlinson 1999; Kumaraswamy & Matthews 2000). Project partnering is partnering undertaken on a single project. At the end of the project, the partnering relationship is terminated and another relationship is commenced on the next project. Project partnering was pioneered in the USA construction industry during the mid to late 1980s. Australia followed suit by adopting the partnering philosophy in the early 1990s. Strategic partnering takes place when two or more firms use partnering on a long-term basis to undertake more than one construction project, or some continuing construction activity (RCF 1995). Kubal (1994) and more recently the Reading Construction Forum (1998) discuss partnering at an industry-wide level. Kubal (1994) notes that although partnering is practiced on fragmented projects, it required national lobbying in order for partnering to be used across industry under the correct circumstances. In the UK, the Reading Construction Forum (1998) develop this point further by stating that new initiatives in partnering have enabled "second and third generation partnering" to evolve. Watson (1999) reported that second generation partnering was underpinned by the "seven pillars" of partnering (RCF 1998) which are strategy, membership, equity, integration, benchmarks, project processes, and feedback. In the third generation of partnering, the construction firm should be building virtual organizations with its supply chain to provide a complete service that is efficient, creative, and innovative (Watson 1999; Kumaraswamy & Matthews

2000). The industry should also become truly collaborative in producing and marketing a range of services that clients are eager to invest in (Matthews & Rowlinson 1999). Figure 1 shows the three categories of partnering as described by Reading Construction Forum (1995, 1998).

***Project and Strategic Partnering***
*Partnering can be applied to one-off schemes (project partnering), or can be on going over a series of developments (strategic partnering).*

*Typically, with project partnering, cost savings of 2-10% are achieved, with strategic partnering savings of 30% are realistic overtime.*
(RCF, 1995:iii)

***Key Principles***
- *Agreeing mutual objectives.*
- *Making decisions jointly and resolving problems.*
- *Aiming at targets that provide continuous measurement in performance from project to project.*

(RCF, 1998: Chp. 1, Page 3)

***Second Generation***
*A 'Second Generation' of partnering has now emerged that requires a strategic decision to cooperate in improving joint performance by a client and a group of consultants, contractors and specialists engaged in an ongoing series of projects… Second generation is tough but hose forms who have the Seven Pillars in place find that cost savings of 40% are not uncommon, and time savings of more than 50% are achievable.*
*(RCF, 1998:iii)*

***Key Principles (Seven Pillars)***
*Strategy, Membership, Equity, Integration, Benchmarks, Project Process, Feedback.*
(RCF, 1998, Chp. 3, Page 12)

***Third Generation***
*…research also identifies the beginnings of a third generation of partnering in which the construction industry becomes a truly modern industry productING and maketing a range of products and services that clients are eager to invest in. The resulting Third Generation Partnering delivers even greater benefits, - cost savings of more than 50% or more, and where speed is crucial, construction time frames can be reduced by 50% or more.*
*(RCF, 1998:ii)*

*Fig. 2: Evolution of partnering: from project to third generation (adapted from RCF 1995, 1998 by Matthews & Rowlinson 1999 – p.349)*

A comparison of identified partnering elements is listed as follows:

| Associated General Contractors of America (1991) | Sanders and Moore (1992) |
|---|---|
| Commitment<br>Continuous evaluation<br>Equity<br>Mutual objectives<br>Timely responsiveness<br>Trust<br>Implementation | Cooperative management team<br>Cooperation<br>Open communication<br>Group working<br>Common goals<br>Problem solving |
| **Matthews (1996)** | **Reading Construction Forum (1995)** |
| Goals and objectives<br>Trust<br>Problem resolution<br>Commitment<br>Continuous evaluation<br>Group working<br>Win-win philosophy<br>Shared risk<br>Equity<br>Cooperation | Free and open communication<br>Open book costing<br>Annual review of performance<br>Workshops<br>Continuous evaluation<br>Mutual objectives<br>Problem resolution |

*Fig. 3: Comparison of Identified Partnering Elements (Adapted from Matthews 1996 by Kumaraswamy & Matthews 2000 – p.5)*

Green (1999) offers a counter view on partnering. He argues that the philosophy of continuous, measured improvement from the definition of partnering presented by Construction Industry Board (1997) actually demands that each project exceeds the performance of the previous one. Despite the seductive discourse on "empowerment", "working together" and "relationships", the ultimate measure of success seems to hinge on cost improvement.

Green (1999) also suggests that the arguments in favour of partnering would seem to owe more to the buying power of its advocates rather than to any independent appraisal. It is made clear by the Construction Clients' Forum (1998):

"…the message from the Construction Clients' Forum is clear. If this Pact is concluded, clients represented on the CCF will seek to place their £40bn of business with companies that are seen to follow the approach described in this document…"

Construction Industry Board (1997) has also made their point equally clear:

"…if it becomes clear that anyone at the workshop is unable to adopt the spirit of partnering, that person should be replaced in the team…"

Green (1999) has further pointed out that the propagation of partnering in construction is to exercise increased control over the construction supply chain. Examples of some leading supermarkets in U.K. were used and Green (1999) suggested that their innovations in supply-chain management are directed towards earning super-normal profits, rather than serving the interests of their customers. Investigation was carried out by the Office of Fair Trading in 1998 according to The

Times report on 31 July 1998. Further investigation of the supermarkets was carried out by Monopolies and Mergers Commission in late March 1999, facing monopoly penalty**.**

It is difficult to separate partnering from the principles of TQM because they both share a common goal – continuous improvement, which originally came from TQM (Green, 1999). TQM encourage employees to identify themselves as parts of a supply chain which comprises a sequence of relationships between suppliers and customers (Tuchman, 1995). Kerfoot and Knight (1995) suggest that this provides employees with a sense of self-esteem from serving the next person in the chain, rather than having to derive satisfaction from the task itself. Metaphors such as "teamwork" and "customer" are therefore intentionally used to mask the reality that most employees are required to act as mindless cogwheels in a remorseless machine (Green, 1999). If this critical interpretation is accepted, Green argues that the rhetoric of customer responsiveness is primarily used as hollow propaganda to justify management regimes which are increasingly based on domination and control. The more that managers' behaviour is governed by propaganda, the less likely they are to engage in risk-taking and entrepreneurial behaviour.

Wood et al. (2002) and Wilson (1994) find the essence of partnering is single-source, long-term relationships. Such relationships are business-focused; directed at solving problems, rather than simply selling products. Trust is a key component when a new relationship is developed with the industry moves from competitive, adversarial to cooperative relations based on reciprocity and solidarity (Wood & McDermott 1999). Trust-based partnering encourages parties to adopt higher ethical standards.

# Alliancing

Confusion on the differences between partnering and alliancing is common in the construction industry. The most notifiable distinction between partnering and alliancing is described by Walker & Hampson (2003) as:

"…with partnering, aims and goals are agreed upon and dispute resolution and escalation plans are established, but partners still retain independence and may individually suffer or gain from the relationship. With alliancing the alliance parties form a cohesive entity, that jointly shares risks and rewards to an agreed formula…"

Alliancing is categorised into two main types by scholars, namely strategic alliancing and project alliancing. The most common definition of strategic alliances adopted is to establish inter-organizational relations and to engage in collaborative behaviour for a specific purpose (Love et al., 1999). The inter-organisational relationships can be grouped into three broad classifications of services: cross-company consortium (service), opportunistic and stakeholder alliances (Howarth et al., 1995). A strategic alliance is also seen as an inter-organisational arrangement which usually exists between two companies that extends beyond a specific project and the parties would expect ongoing, mutually beneficial business (Peters et al., 2001). According to Bronder and Pritzl (1992), a strategic alliance exists when the value chain between at least two organizations with compatible goal structures are combined for the purpose of sustaining and achieving significant competitive advantages.

| | |
|---|---|
| Service Alliances | • Requires the lowest level of interdependence between partners with the smallest amount of changes and the lowest level of joint commitment<br>• Provide economies of scale<br>• Provide the ability for the partners to undertake large-scale projects with a limited purpose<br>• Difficulties arise due to the diversity of the interests and goals of the partners<br>• Result in a loss of commitment from members |
| Opportunistic Alliances<br>e.g. Joint Venture | • Provide access to the resources of the partner organizations<br>• Motivated by the existence and recognition of a market opportunity<br>• Partners might exploit one another's resources and then move on to pursue the opportunity alone |
| Stakeholder Alliances<br>e.g. Suppliers, customers, employees. | • The closest link between member organizations of all<br>• Seek to build strong, long-term relationships<br>• Assist in achieving the organizational goals by major stakeholders |

*Fig. 4: Characterises of services, opportunistic and stakeholder alliances (Adapted from Howarth et al. 1995)*

A strategic alliance can provide access to resources such as capital, information, technology, management expertise, markets, customers, distribution channels, land and labour. Such resources may not be available to an organization acting alone.

Greater access to resources allows an organization to reduce its level of uncertainty in a demanding and turbulent environment. Strategic alliances also enable organizations to speed up the market-entry process and increase their responsiveness to consumer markets (Howarth et al., 1995).

Yet, no successful strategic alliances can be developed without trust. Trust in a strategic alliance also includes the concept of reciprocity, which implies a long-term focus, the acceptance that obligations are mutual, and room for adjustment if one partner is suddenly placed in a compromising position (Howarth et al., 1995). Like partnering and relational contracting, trust between strategic alliance partners is important because it creates an opportunity and willingness for further alignment, reduces the need for partners to continually monitor one another's behaviour, reduces the need for formal controls, and reduces the tensions created by short-term inequities. It allows the partners to focus on their long-term business development as well as cutting down their cost and time. The characteristics of successful strategic alliances as well as successful business relationships proposed by Hampson and Kwok (1997) – trust, commitment, interdependence, cooperation, communication and joint problem solving – reflect a similar theme.

A successful alliance also requires creativity. It has been shown in the past that alliances that have failed are typically the second alliance that a group of companies undertake together. The problem arises when the individual team members who were on the first alliance insist on using the same practices by repeating them since they worked on the previous alliance, despite the fact that they might not be appropriate for the second. The new team members do not understand why the practices are adopted and do not feel any sense of ownership. Since both strategic and project alliances are tailor-made mechanisms, such alliancing would fail due to the lack of creativity by the team members from the first project team and the new team members do not feel committed to work.

The main difference between project alliances and strategic alliances is project alliances have a defined end, which is most commonly the practical completion date of a project. The parties are brought together for a specific project or outcome (Peters et al., 2001). A project alliancing agreement is also legally enforceable.

A project alliance is described by Hutchinson & Gallagher (2003) as a project delivery strategy, several participants join together to share risks and outcomes on a project (Manivong & Chaaya, 2000), where sponsor and commercial participants' objectives (client's objectives) are aligned to:

- Maximise performance;
- Proactively manage risk;
- Reduce cost; and
- Achieve outstanding results in sponsor key project objective.

Hutchinson & Gallagher (2003) defines project alliance as:

"… an integrated high performance team selected on a best person for the job basis; sharing all project risks with incentives to achieve gamebreaking performance in pre-aligned project objectives; within a framework of no fault, no blame and no dispute; characterised by uncompromising commitments to trust, collaboration, innovation and mutual support; all in order to achieve outstanding results."

Love and Gunasekaran (1999) stated alliances can be either collaborative or cooperative (Bronder and Pritzl, 1992; Hamel, 1989; Hutchinson & Gallagher, 2003) based on core competences. Kwok et al. (1996) describe project alliances as a cooperative arrangement between two or more organisations that forms part of their overall strategy, and contributes to achieving their major goals and objectives for a particular project. Hamel (1989) suggests that organizations that enter into collaborative alliances (short-term) are aware that their partners are capable of disarming them. Parties to these alliances have clear objectives and understand that their partner's objectives will affect their success. Yet, collaboration does not always provide an opportunity to internalize a partner's skills. Love and Gunasekaran (1999) suggest that a "psychological barrier" may exist between alliance partners caused by the fear that their partner(s) may out-learn or deskill them. Wood and Gray (1991) state that organizations typically enter collaborative relations to reduce the complexity of their environment and to gain more control over environmental factors. Such collaboration may cause new dependencies to be created, which may increase environmental complexity and turbulence. They argue that increases in complexity may increase transaction costs, the need to manage bilateral and multilateral relations and the need to develop new skills.

Cooperative alliances (long-term) encourage alliance partners to commit their resources to the relationship to gain mutual learning (Love et al., 1999). There is a lower level of competition and as a result, partners may feel more committed to work together and exchange their knowledge and resources. Ketelholm (1993) suggests that cooperative strategic alliances can create a competitive advantage. Organizations that rely on cooperation have been found to obtain lower costs for as long as they maintain trust internally and externally – among employees and members of their network.

## Relational Contracting

Relational (or relationship) contracting is based on a recognition of mutual benefits and win-win scenarios through more cooperative relationships between the parties. Relational contracting embrace and underpin various approaches, such as partnering, alliancing, joint venturing, and other collaborative working arrangements and better risk sharing mechanisms (Alsagoff & McDermott, 1994; Jones, 2000; Rahman & Kumaraswamy 2002). Relational contracts are usually long-term, develop and change over time, and involve substantial relations between the parties. Relational contracts are the norm for complex transactions to be conducted in environments of high complexity, where complete contingency arrangements are impossible. Successful completion of the transaction relies on the cooperation and the desire to effectuate the contract. In addiction, the contract must allow certain flexibility so as to enable necessary adjustments as appropriate (Cheung, 2001). The characteristics of relational contracts and construction contracts are summarized below:

| | **Relational Contracts** | **Construction Contracts** |
|---|---|---|
| Contracting Environment | • Cooperative instead of defensive.<br>• Proactive instead of reactive. | • Cooperative, mutual trust is the desired static of contracting |
| Effectuation | • Flexibility and Adjustments provisions to cater for unanticipated contingencies. | • Power to issue variations with associated time and cost adjustments |
| Dispute Resolution | • Relational Dispute Resolution. | • Alternative Dispute Resolution |

*Fig. 5: Characteristics of Relational Contract and Construction Contract (adapted from Cheung 2001 – p.43)*

Various authors have suggested that a relational approach to contractual governance entails long-term social exchange between parties, mutual trust, interpersonal attachment, commitment to specific partners, altruism and cooperative problem solving (Blau, 1964; MacNeil, 1978, 1985; Rousseau and Parks, 1993; Darwin, 1994; Darwin et al., 2000). Darwin and numerous of authors suggested that a relational approach is closely associated with partnerships and strategic alliances (Jorde and Teece, 1989; Kanter, 1989, 1994; Lynch, 1993) with contractors who avoid adversarial approaches to contract management (e.g. Lorenz, 1991; Stinchcombe, 1986; Teubner, 1991) by emphasizing the "stable bonding mechanisms" (Bolton et al., 1994) which entail long-term collaborative arrangements based on informality, shared problem solving, reciprocity and high trust. MacNeil (1995) suggested that construction contracts are typical relational contracts as construction contracts often involve numerous parties and subcontracts with heavy informational exchange in the construction activities. The parties involved are mutually dependent to each other. The extent of mutuality and interdependence and the need for trust and cooperation are greatly heightened (Cheung, 2001).

According to Rahman and Kumaraswamy (2002), relational contracting considers contracts as the "ongoing dynamic state" of relations among the contracting parties and promises to do something in the future (MacNeil, 1974), in the process of projecting "exchange" into the future (MacNeil, 1980). Rahman and Kumaraswamy (2002) point out that no real life human cooperation will be found entirely transactional, personal relations, diffuse communication and some non-economic personal satisfaction will be involved. And so will contractual relations not be found entirely lacking in transactional discreteness. Accordingly, MacNeil (1978) classified contracts into three types: classical, neoclassical, and relational. Classical contracting covers all future contingencies, and transactions tend to be self-liquidating. Neoclassical contracting involves trilateral governance, where third-party "assistance" is employed in resolving disputes and evaluating performance. Relational contracting provides the means to sustain ongoing relations in long and complex contracts by adjustment processes of a more thoroughly transaction-specific, ongoing administrative kind.

Industry-wide studies have pointed out that a more efficient construction industry would be achieved if a cooperative style of contracting is used. Two major studies in quality and efficiency of the construction industry commissioned by the government were carried out in the UK. The Latham Report (1994) highlighted 30% reduction in construction costs as an attainable goal while the Egan Report (1998) foreseen an annual reductions of 10% in both construction costs and time. The common theme in their recommendations is replacement of competitive tendering with long-term relationships.

Partnering is a good example of practicing relational contracting principles (Rahman and Kumaraswamy, 2002). Thompson and Sander (1998) observed that benefits from partnering (i.e. relational contracting) increase with a migration of teamwork attitude from competition to cooperation, through to collaboration and finally to coalescence. Rahman et al. (2001) argued that more relational and performance oriented contractor selection would encourage an amicable relational contracting environment and more collaborative teamwork. Rahman and Kumaraswamy (2002) suggest relational contracting approaches are expected to work in almost any environment if applied properly. However, this requires transforming traditional relationships towards a shared culture that transcends organizational boundaries (CII, 1996) where the motivation and attitude of the project participants are also critical.

# Post script: Future Directions

Alliancing, partnering and relational contracting, all have a common theme, which is to develop a long-term relationship for such to be applied successfully. From the previous literature review, it is not difficult to see that both alliancing and partnering are heading toward the concept of Relational Contracting. Long-term relationship has always been a main element in Relational Contracting. In order to build up a long-term relationship between two parties, trust is something one cannot miss.

Unlike traditional contracting, relational contracting allows a much higher flexibility which is suitable for the construction industry. In the construction industry, there are many uncertainties as well as many unforeseeable events. With relational contracting, a lower construction cost can possibly be obtained. With traditional contracts, if contractors are not able to get their work done on time according to the contract, they will suffer liquidated damages and in most cases, arbitration or litigation will also be involved. Because of the involvement of legal practitioners, works may delayed and the construction time extended since work will be postponed until proceedings and procedures have been carried out and results have been known. For example, it is not uncommon for an arbitration to take at least one year before the decision is made.

With the high flexibility in relational contracting, construction time will be shortened due to less documentation passing between parties when an unexpected event has occurred during construction; solutions will be negotiated around a table. Also, it might minimize the necessity of extensions of time for works since the contractor has a higher flexibility in the ways it may put forward the work.

Without the aggravation of hearings, claims and damages, a better relationship is built up between the client and the contractor. The trust in each other has become stronger and the contractor is willing to work for the client in a better and more efficient way where the client is willing to give the contractor more works with it at the top of the pick list for future jobs. A mechanism for dealing with this used in Hong Kong government contracts is the appointment of an alternative dispute resolution adviser. The role is one of arbiter between the two parties but this is still, essentially, an adversarial approach – although a skilled advisor can draw the parties together into an informal, relational approach. Such a role could be fitted “on top” of a relational contract to help steer it after the project workshop has been completed.

However, despite the fact of moving towards long-term relationship, a recent case study carried out by Darwin et al. (2000) on ten clients from public sector and contractors in the U.K., shows that it is not desirable to have pure long-term relationship from both clients’ and contractors’ point of view, but it is also necessary to have black and white contracts between them.

Due to the human nature, while moving along with the main purpose of relational contracting, legal binding documents are also necessary for both parties to feel secure and ensure work is to be “guaranteed”. Also, for the public sector, a transparent system is required and the government needs to report to the public. Such as “what if that does not happen…” some terms in black and white are needed to provide comfort for society.

Pure “buddy buddy” relationships do not exist in the commercial world. There is not complete trust.

Culture is another issue.  Without knowing much or having a lot of work experience with the contractor, the client may have a query in its mind over trusting the contractor.  One may argue there is pre-qualification, however, further research may be carried out on effectiveness of pre-qualification in respect of relational contracts.

Contractors have traditionally always taken every single chance to increase their income during work, and this has been part of the culture in the construction industry – see, for example, the CIRIA report on management contracting.  However, if once the contractor knows there will be more work with the client in the future, it is highly likely that he would look at the relationship from a long-term prospective rather than concentrating on grabbing more money during work in a short-term response.

It is interesting to see that many centuries ago, everything was simple and people had a much stronger sense in trusting one another.  Where as now, every party tries to get the most out of the other.  Because of such human behaviour, workshops evolve with the aim of trying to build up the team spirit as well as trusting in each other.  Yet, the objectives of the workshops need to be implemented continuously or the results will fade and the whole program will become a failure.  In this case, it depends very much on the company approach on future development and implementation.

After all, “Business is business”, which also describes the current industry culture as a whole.

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### *Appendix I: Transactional and Relational Contracting (adapted from Darwin et al. 2000 – p.41)*

| Transactional pole | Relational pole |
|---|---|
| Communication is limited and formal | Communication is extensive, and is both formal and informal |
| Everything is measured in monetary terms | Many aspects are difficult to measure, either in monetary or in other terms. Parties do not measure them |
| The beginning and end of the contract relationship are clearly defined | The beginning and end, if any, of the contract relationship are gradual |
| Initial planning is complete and specific – only remote contingencies are not covered | There is limited specific planning at the beginning |
| There is little or no bargaining as the contract proceeds | The contract involved extended mutual planning – a "joint creative effort" |
| The contract agreement binds the partners totally | The agreement is tentative |
| Almost no cooperation is required after the start of the contract | The success of the contract is entirely dependent on further cooperation in both performance and further planning |
| Each particular benefit and burden is specifically assigned to one party | There is undivided sharing of both benefits and burdens |
| Specific rules and rights are applicable, based on agreement. These are usually measured in monetary terms | Rules and benefits are non-specific and non-measurable |
| No altruistic behaviour is expected or occurs | There is significant expectation of altruistic behaviour |
| Problems in performance or among the participants are not expected, except perhaps those planned for. If they occur, they are expected to be governed by specific rights | The possibility of trouble is anticipated and is dealt with by cooperation |

## *Appendix II: Definitions of Partnering, Alliancing and Relation Contracting*

| PARTNERING | ALLIANCING | RELATIONAL CONTRACTING |
|---|---|---|
| **Queensland Government – Dept. of Main Roads**<br>• not a form of contract<br>• a process applied outside the contract to align the goals and objectives of the contract parties<br>• to facilitate good communication, teamwork and joint problem solving<br>• can be used in conjunction with any form of contract<br>• not necessarily legally binding<br>• a way of conducting business in which two or more organizations make long-term commitments to achieve mutual goals | • (project alliance) an agreement between two or more entities that undertake to work co-operatively<br>• share project risk and reward between parties<br>• achieve agreed outcomes based on principles of good faith and trust, with an open book approach towards cost<br>• a purpose built contract in which the client and the contractor form an alliance to build the works<br>• both parties develop and agree on the target cost estimate for the project<br>• a board drawn from both organizations manages the contract | • not a form of contract<br>• a good relationship between two or more parties that contributes towards the successful completion of a contract<br>• the provision of a collaborative or team approach to the achievement of project outcomes that are best for the project |
| **Construction Best Practice Programme**<br>• a structured management approach to facilitate team working across contractual boundaries<br>• fundamental components include mutual objectives, agreed problem resolution methods and an active search for continuous measurable improvements | **Bronder & Pritzl**<br>• exists when the value chain between at least two organizations with compatible goal structures are combined for the purpose of sustaining and achieving significant competitive advantages<br>• can be collaborative or cooperative | **Cheung**<br>• cooperative and proactive contracting environment<br>• flexibility and adjustments provisions to cater for unanticipated contingencies<br>• relation dispute resolution<br>• parties are mutually dependent to each other<br>• trust and cooperation are greatly heightened |
| **European Construction Institute, Liu & Fellows**<br>• a method of improving communication mechanisms and technologies<br>• a method of responding to innovative construction<br>• creates a less stressful working environment<br>• reduces transaction costs resulting from uncertainty, competition and information asymmetry | **Wood & Gray**<br>• organizations enter collaborative relations<br>• to reduce the complexity of their environment<br>• to gain more control over environmental factors<br>• may create new dependencies<br>• may increase environmental complexity and turbulence<br>• may therefore increase transaction costs | **Blau, MacNeil, Rousseau & Parks, Darwin, Darwin *et al.***<br>• entails long-term social exchange between parties<br>• mutual trust<br>• interpersonal attachment<br>• commitment to specific partners<br>• altruism<br>• cooperative problem solving |

## PARTNERING

**Construction Industry Institute**

- experimental partnering, packaged partnering and committed partnering
- a long-term commitment between two or more organizations for the purpose of achieving specific business objectives by maximizing the effectiveness of each participant's resources
- requires changing traditional relationships to a shared culture without regard to organizational boundaries
- relationship is based on **trust**, dedication to common goals and an understanding of each other's individual expectations and values

## ALLIANCING

**Howarth, Gillin & Bailey**

- service alliances
    - requires the lowest level of interdependence between partners with the smallest amount of changes and the lowest level of joint commitment
    - provide economies of scale
    - provide the ability for the partners to undertake large-scale projects with a limited purpose
    - difficulties arise due to the diversity of the interests and goals of the partners
    - result in a loss of commitment from members
- opportunistic alliances
    - Provide access to the resources of the partner organization
    - Motivated by the existence and recognition of a market opportunity
    - Partners might exploit one \another's resources and then move on to pursue the opportunity alone
- stakeholder alliance
    - the closest link between member organizations of all
    - seek to build strong, long-term relationships
    - assist in achieving the organizational goals by major stakeholders

## RELATIONAL CONTRACTING

**Alsagoff & McDermott, Jones, Rahman & Kumaraswamy**

- based on recognition of mutual benefits and win-win scenarios through more cooperative relationships between parties
- embrace and underpin various approaches such as:
    - partnering
    - alliancing
    - joint venturing
    - collaborative working arrangements
    - better risk sharing mechanisms
- long-term
- develop and change over time
- involve substantial relations between parties
- the norm for complex transactions to be conducted in high complexity environments, where complete contingency arrangements are impossible

| PARTNERING | ALLIANCING | RELATIONAL CONTRACTING |
| --- | --- | --- |
| **Green**<br>• concerns with maximizing effectiveness<br>• demands each project exceeds the performance of the previous one<br>• measure of success hinges on cost improvement<br>• more onto the buying power than to any independent appraisal<br>• to exercise increased control over the construction supply chain<br>• common goal with TQM – continuous improvement | **Hamel**<br>• can be collaborative or cooperative<br>• collaborative alliances<br>    ○ organizations aware that their partners are capable of disarming them<br>    ○ clear objectives<br>    ○ understand partner's objective will affect their success | **Darwin, Jorde & Teece, Kanter, Lynch, Bolton *et al.***<br>• closely associated with partnerships and strategic alliances<br>• especially with contractors who avoid adversarial approaches to contract management<br>• entail long-term collaborative based on<br>    ○ informality<br>    ○ shared problem solving<br>    ○ reciprocity<br>    ○ high trust |
| **Bennett and Jayes**<br>• a management approach used by two or more organizations to achieve specific business objectives by maximizing the effectiveness of each participant's resources<br>• mutual objectives between organizations<br>• agreed method of problem resolution<br>• an active search for continuous measurable improvements | **Love & Gunasekaran**<br>• can be collaborative or cooperative<br>• collaborative alliancing<br>    ○ help to establish the inter-organizational relations<br>    ○ organizations engage in collaborative behaviour for a specific purpose<br>    ○ a "psychological barrier" may exist between partners<br>    ○ may fear that their partners may out-learn or deskill them<br>• cooperative alliances<br>    ○ encourage partners to commit their resources to the relationship to gain mutual learning<br>    ○ lower level of competition<br>    ○ partners feel more committed to work together<br>    ○ partners exchange their knowledge and resources | **MacNeil**<br>• construction contracts are typical relational contracts<br>• involve numerous parties and subcontracts with heavy informational exchange in the construction activities<br>• parties are mutually depend to each other<br>• provides the means to sustain ongoing relations in long and complex contracts by adjustment processes of a more thoroughly transaction-specific, ongoing administrative kind |

| PARTNERING | ALLIANCING | RELATIONAL CONTRACTING |
|---|---|---|
| **DETR**<br>• involves two or more organizations working together to improve performance through agreeing mutual objectives<br>• devises a way for resolving disputes<br>• commits themselves to continuous improvement<br>• measures progress<br>• shares the gains<br>• a tool to tackle fragmentation | **Hutchinson & Gallagher**<br>• an integrated high performance team selected on a best person for the job basis<br>• sharing all project risks with incentives to achieve gamebreaking performance in pre-aligned project objectives<br>• a framework of no fault, no blame and no dispute<br>• uncompromising commitments to trust, collaboration, innovation and mutual support<br>• objective is to achieve outstanding results | **Rahman & Kumaraswamy**<br>• “ongoing dynamic state” of relations among the contracting parties<br>• promises to do something in the future, in the process of “exchange” to the future<br>• involve transactional discreteness<br>• partnering practices relational contracting principles |
| **Construction Industry Board**<br>• establishment of agreed and understood mutual objectives<br>• methodology for quick and cooperative problem resolution<br>• culture of continuous, measured improvement | **Hampson & Kwok**<br>• successful strategic alliances<br>  ◦ trust<br>  ◦ commitment<br>  ◦ interdependence<br>  ◦ cooperation<br>  ◦ communication<br>  ◦ joint problem solving | |
| **Peters, Walker & Hampson**<br>• relies solely on the commitment of individuals<br>• not legally binding<br>• aims and goals are agreed<br>• dispute resolution and escalation plans are established<br>• partners retain independence<br>• partners may suffer or gain from the relationship individually | • 2 types of alliancing – strategic alliancing and project alliancing<br>• parties form a cohesive entity<br>• parties shares risks and rewards according to an agreed formula<br>• strategic alliance<br>  ◦ inter-organisational arrangement<br>  ◦ relationship between parties extends beyond a specific project<br>  ◦ ongoing mutually beneficial business<br>• project alliancing<br>  ◦ defined end<br>  ◦ parties brought together for a specific project<br>  ◦ legally enforceable | |

| PARTNERING | ALLIANCING | RELATIONAL CONTRACTING |
|---|---|---|
| **Gaede, Reading Construction Forum, Matthews, Matthews & Rowlinson, Kumaraswamy & Matthews**<br>• categorized as project partnering and strategic partnering<br>• project partnering<br>  ○ undertaken on a single project<br>  ○ partnering relationship terminated at the end of project and new relationship commenced on the next project<br>• strategic partnering<br>  ○ takes place when two or more firms use partnering on a long-term basis<br>  ○ usually undertaken in more than one project or continuing construction activity | | |
| **Watson, Reading Construction Forum**<br>• second generation partnering<br>• “seven pillars” – strategy, membership, equity, integration, benchmarks, project processes, feedback<br>• strategic decision | **Manivong & Chaaya**<br>• project alliancing<br>  ○ a project delivery method<br>  ○ several participants join together to share risks and outcomes on a project | |

**Kubal**

- required national lobbying in order for partnering to be used across industry

**Kwok et al.**

- project alliance
  - a cooperative arrangement between two or more organizations
  - forms part of the organisations' overall strategy
  - contributes to achieving their major goals and objectives for a particular project

**Watson, Kumaraswamy & Matthews, Matthews & Rowlinson**

- third generation partnering
- construction industry should be building virtual organizations with its supply chain to provide a complete service that is efficient, creative and innovative
- collaborative in producing and marketing a range of services that clients are eager to invest in
- cost saving
- construction time reducing

**Wood & McDermott, Wilson & Wilson**

- single-source, long-term relationships
- business-focused
- directed a t solving problems, rather than simply selling products
- trust is a key component
- industry moves from competitive, adversarial to cooperative relations based on reciprocity and solidarity
- encourages parties to adopt higher ethical standards with trust-based partnering

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