

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

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### **Abstract**

Construction project teams are unique entities, created through a complex integration of factors, with inter-disciplinary players, varying roles, responsibilities, goals and objectives (Goodman and Chinowsky, 1996). Collaboration and teamwork are therefore crucial since sharing up-to-date information between participants leads to minimising errors, reduction of time delays and breaking the widespread rework cycle, which allows a sustainable relationship between participants to evolve. Benefits of collaborative, rather than adversarial, working relationships within construction organisations are well documented (Walker and Hampson, 2003).

Successful sustainable relationships rely on relational forms of exchange characterised by high levels of trust. However, it was shown in the past that the construction industry has a stronger preference for distrust rather than the full benefits of cooperation (Wood and McDermott, 1999). There is a need for culture change to bring about increased cooperation between parties on a long-term basis. With relational contracting, based on the sustainable relationship and trust, a win-win situation can be created for both the client and contractor. The development of trust between organisations is seen as a function of the length of the relationship between them (Bresnen and Marshall, 2000a). It is also believed that the construction industry is one which requires lots of trust between participants due to the high uncertainty in the industry.

This paper aims to look at the how traditional procurement methods are changing and moving towards sustainable procurement forms through the relational contracting approach. A critical review on first and second generation partnering will be presented, followed by a discussion of how change in procurement culture, towards sustainable business relationships, can be investigated.

### **Keywords**

Collaboration, teamwork, sustainable relationship, procurement, culture

### **1. 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 paper aims to review existing definitions of these three concepts and present an overview of the current state-of-the-art in terms of their use and implementation.

## **2. 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 (Walker & Hampson, 2003:48). Partnering is also recognised 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 produced by CII as follows (CII, 1991):

“...a long-term commitment between two or more organisations for the purpose of achieving specific business objectives by maximising the effectiveness of each participant’s resources. This requires changing traditional relationships to a shared culture without regard to organisational 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 the 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 organisations to achieve specific business objectives by maximising 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.”

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 Figure 1 shows the three categories of partnering as described by Reading Construction Forum (1995, 1998).

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 equally clear by the Construction Clients' Forum (1998) and Construction Industry Board (1997). 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.

### **3. 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-organisational 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 as shown in table 3 below. 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 organisations with compatible goal structures are combined for the purpose of sustaining and achieving significant competitive advantages.

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). 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. 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). It is also described by Hutchinson and Gallagher (2003) as a project delivery strategy, several participants join together to share risks and outcomes on a project (Manivong and Chaaya, 2000). Also, a project alliancing agreement is legally enforceable.

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 and Hampson (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 organisations 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 internalise 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) also state that organisations typically enter collaborative relations to reduce the complexity of their environment and to gain more control over environmental factors.

Cooperative alliances (long-term) encourage alliance partners to commit their resources to the relationship to gain mutual learning (Love and Gunasekaran, 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. Organisations 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.

#### 4. 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 embraces and underpins various approaches, such as partnering, alliancing, joint venturing, and other collaborative working arrangements and better risk sharing mechanisms (Alsagoff and McDermott, 1994; Jones, 2000; Rahman and Kumaraswamy 2002). In addition, 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 summarised below:

**Table 1: Characteristics of Relational Contract and Construction Contract (adapted from Cheung 2001 – p.43)**

	<b>Relational Contracts</b>	<b>Construction Contracts</b>
Contracting Environment	<ul style="list-style-type: none"> <li>• Cooperative instead of defensive.</li> <li>• Proactive instead of reactive.</li> </ul>	<ul style="list-style-type: none"> <li>• Cooperative, mutual trust is the desired static of contracting</li> </ul>
Effectuation	<ul style="list-style-type: none"> <li>• Flexibility and Adjustments provisions to cater for unanticipated contingencies.</li> </ul>	<ul style="list-style-type: none"> <li>• Power to issue variations with associated time and cost adjustments</li> </ul>
Dispute Resolution	<ul style="list-style-type: none"> <li>• Relational Dispute Resolution.</li> </ul>	<ul style="list-style-type: none"> <li>• Alternative Dispute Resolution</li> </ul>

#### 5. Post Script: Research into pre-requisites for successful relational contracting

The implicit link between organisational culture and organisational performance has long been recognised in both mainstream management literature (Handy, 1985; Hofstede, 1980) as well as in the construction management literature (Liu and Fellows, 2001; Rowlinson, 2001). Within the construction research domain, the impact of culture and organisation on project performance is becoming an increasingly important topic for the establishment of a sound alliancing approach to projects. However, the efficacy of alliancing is so far unproven and this research aims to shed light on the practice and pre-requisites for relational contracting to be successful (see for example Bresnen and Marshall 2000a, b, c). A number of characteristics have been identified in recent studies e.g. Rowlinson, 2001, Winch et al 1997 and 2000. These studies addressed innovation and change in the context of the working relations in project organisations. The main parameters identified as being significant in shaping how an organisation performed and the “spirit” within the organisation were: National culture; Organisational culture; Organisational assessment; Commitment. In addition, Walker et al (2002) has investigated cooperative relations on the National Museum of Australia Project and has provided a fifth data collection instrument. Research by Phua (2002) to empirically quantify the impact of culture on project performance has revealed important dimensions of culture’s antecedents and consequences. Building on this earlier work,

this study plans to incorporate the new insights suggested by Phua (2002) in order to establish the external validity of the scales used to measure culture and project performance. By investigating the impact of the various cultural variables on project performance it will be possible to define patterns in which alliancing contracts “work” and other patterns where traditional contracts “work”. By identifying patterns that are central to the success of a project the instruments can be used prior to the alliancing workshop. By being able to plot the position of the various organisations on the different scales it should be possible to highlight mismatches that can then be addressed at the alliancing workshop. The main parameters identified as being significant in shaping how an organisation performed and the “spirit” within the organisation were: National culture (assessed using Hofstede’s VSM); Organisational culture (assessed using Handy’s instrument); Organisational assessment (assessed using Van de Ven’s instrument); Commitment (assessed using Allen & Meyer’s instrument). By way of example, these are the sorts of issues that can be formulated into hypotheses for the research: Organisational culture and organisation structure must be matched if participants are to retain commitment to the organisation – from Rowlinson (2001).

## **6. Conclusions**

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. With the high flexibility in relational contracting, construction time can 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 minimise the necessity of extensions of time for works since the contractor has a higher flexibility in the ways it may put forward the work.

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 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, each 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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