There are in the construction industry at present two types of novation for the situation where a consultant is to be novated from a client to a design and build contractor. These are the "switch" and the "ab initio" forms.

In order to explain the differences between them, it is necessary to start with some basic principles about novation.

**Novation process – rights and obligations**

Novation describes the process by which the two parties to a contract deal with the rights and obligations under that contract. In a consultant's contract, the rights of either party are basically the rights to sue the other. These rights can be assigned to third parties without consent unless the contract provides otherwise. This is referred to simply as "assignment" and happens all the time.

"Obligations" have always been treated differently. In simple terms, the client's obligation is to pay the consultant and the consultant's obligation is to perform the services. These obligations cannot be assigned to a third party without consent unless the contract provides otherwise. The reason for this is clear. The client does not want to wake up one morning to find a totally different consultant (one he has not chosen and of whose experience he has no knowledge) performing the services for which he engaged his original consultant. Similarly, a consultant does not want to have to accept as a new client a person of whom he may have had bad experiences in the past or if that person has no assets with which to pay him.

**New contract**

When rights and obligations are transferred or assigned, this is called "novation". What happens as a result is that the second client steps into the shoes of the first client. In law, the first contract is extinguished and a new contract replaces it – hence the name.

There are circumstances when consultants may be happy to accept a substitution of one client for another, for example when an affiliate company of the client takes over the project.

**Past obligations**

Novation cannot cover obligations already performed, ie the services carried out to date, because these are not going to be re-performed for the new client. The consultant is not going to start his design all over again. Novation will, however, cover the liabilities arising out of the past performance of those obligations. So if a consultant has been negligent before the second client took over, the second client will be able to sue the consultant in respect of that negligence and the first client will not.

It is in this area that the problems concerning novation to a design and build contractor primarily arise. What is the position to be concerning the services that have been performed for the client up to the date of the novation?
**Differences between novation to another client and to a design and build contractor**

It needs to be appreciated that there is a very real difference where the novation is to be to a second client and where the novation is to be to a design and build contractor.

In design/build novation the original client does not drop out of the picture – he continues to carry out the same project. The contractor is to construct that project for the original client and only takes over the consultant’s appointment, not the project itself. The client and the design and build contractor have very different interests:

- the client wants the project carried out to high standards within his budget and timescale and then will sell or use the building;
- the contractor wants to construct the project as efficiently and economically as possible, make a profit and then leave.

In all this, the tender price of the contractor is crucial. The client is looking for a competitive price. The contractor wants to know as accurately as possible what it is going to cost him to build it.

**When novation takes place**

Generally, novation takes place when the building contract is entered into and therefore after the contractor has tendered for the work, but it could take place earlier than that. Also, since it is to be a design/build contract, the contractor at that stage will be taking over responsibility for some or all of the design.

**What is being novated**

What is being novated at that time – only the obligations under the original appointment that have yet to be performed by the consultant. This could be, at one end of the scale, when nearly all the design has been completed, or at the other end when the design is still at a preliminary stage – for example, only that necessary to put together the Employer’s Requirements.

To repeat, obligations that have already been performed cannot be novated unless the consultant is to do them again.

**Nature of liability arising out of services performed prior to novation**

As to the liabilities arising out of the design or other services carried out prior to novation, ie in respect of obligations already performed by the consultant: these can only ever have been performed for the original client even if the design and build contractor may now take the benefit of them – that is, will now be able to sue the consultant in place the original client.

This is because the law says that a consultant does not owe duties in a vacuum. He owes a duty to a particular person and his relationship to that person determines the scope of his duty and thus the kind of loss for which he is liable (and therefore for which he is liable to that person’s assignee: the design and build contractor under a design/build novation).

So the relevant question in law relating to the liability of a consultant for loss arising from his performance prior to novation is *Was it the kind of loss that the consultant owed a duty to his original client to use reasonable skill and care to prevent?*
Blyth & Blyth

It will be apparent from this how the sort of situation highlighted by the Blyth & Blyth case arose. There the engineers had done some design for the client. The contractor used the engineers’ information in the Employer’s Requirements prior to tender to estimate how much steel reinforcement would be needed and costed on that basis. Thereafter, the building contract was let and the engineers novated. The contractor then discovered that much more steel reinforcement was needed and sued the engineers on the basis of alleged deficiencies in the Employer’s Requirements which resulted in their tender price being too low. As the design and build contractor had accepted responsibility for the design he had to bear this loss and could not recover it from the client.

However, the court said this was not the kind of loss the engineers were under any duty to their client to use reasonable skill and care to avoid. Consultants may advise clients on aspects concerning tenders but they do not become responsible to the client if the design and build contractor makes insufficient allowance for any particular item in his tender as this is not a loss the client will suffer.

The judge said in that case that to make Blyth & Blyth responsible to the design and build contractor in these circumstances would involve a retrospective recasting of their duty of care so that it was owed to the contractor and not to the client, and the novation agreement in that case had not achieved that.

Nub of the debate

This brings us to the central point of the whole debate about ab initio and switch novation agreements. It is really an argument about to whom and in respect of what should the consultant be liable in respect of services performed prior to the actual novation.

Novation ab initio

Design/build novation “ab initio”, the standard form for which is produced by the CLLS, is based is on the traditional form of novation, when the first client transfers his interest in the project to a second client and the second client steps into the shoes of the first client as far as the consultant’s appointment is concerned and is treated as if he was always a party to that contract, in place of the first client.

But the way in which these “ab initio” forms seek to make the consultant liable to the contractor for services carried out for the client prior to the novation is to create the fiction that the consultant’s client has been the contractor from the beginning – the retrospective recasting of the duty of care the judge referred to in the Blyth & Blyth case.

Does this make sense?

This does not make any sense in reality. How can a consultant agree to the legal fiction that he has always worked for the contractor? Up until novation the consultant is working to the requirements of his client and he should have his interests only in mind.

He has not in fact been employed by the contractor at that time and was therefore under no duty to advise him as to the sufficiency of his tender price, nor as to what contingencies and allowances he should provide in his price. Indeed, had he done so at the time he would have been in conflict with the duties he owed to his client and acting in a manner which was adverse to that client’s interests. He might also have been in breach of his duty of confidentiality to his client.

If, however, the consultant agrees to this retrospective duty of care the contractor will have a remedy if he can show that if he had been properly advised by the consultant, on the basis that the consultant was acting for him at that time, the contractor would not have got his tender price wrong.
Other wording

It is not necessary for the words "ab initio" to be used to create this sort of liability.

There are other ways in which the same result can be achieved. For example the novation agreement could:

- make the consultant give the contractor a warranty that he owed the contractor a duty of care from the outset;
- make the consultant acknowledge that the contractor has relied on all information and advice given to the client;
- contain an acknowledgement that any losses suffered by the design and build contractor were within the contemplation of the consultant when he first entered into his appointment with the client.

These too are all based on fictions.

What is the consultant liable for in respect of services before the novation?

The consultant does not escape all liability for services performed prior to the novation. The design and build contractor will be able to sue the consultant in respect of errors committed prior to novation if it resulted in the kind of loss for which the consultant was under a duty of care to his original client to avoid, for example the cost of repairing defective work resulting from a defect in the consultant's design prior to the novation. But this is a relatively limited protection for a design and build contractor and certainly does not help him if he has got his tender price in relation to the consultant's design wrong.

Clients' position under ab initio novation

Clients are not concerned about the liabilities their consultants incur to third parties – in this case the design and build contractor before he becomes the consultant's employer. They do, however, want their design and build contractor to take on full one-point responsibility for all design and construction, and if an ab initio form of novation agreement helps to achieve this clients will try to procure one from their consultants.

The client's position is not affected either way - having passed over all responsibility to the design and build contractor he has no need to reserve any rights to sue his consultant in respect of any errors that may have been committed prior to novation. (He may of course want a warranty back from the consultant in respect of the post-novation services on a "have your cake and eat it" basis, but that's another story.)

When liability to the contractor can arise outside any novation

Should a consultant, when he is still employed by the client, volunteer advice to the design and build contractor during the tender period and/or answer queries from the design and build contractor on which the contractor relies, then the consultant will be liable to the contractor if he does so negligently on what is know as the Hedley Byrne principle, regardless of any terms in his appointment or any novation agreement. The Galliford Try v Mott MacDonald case in July this year was put on this basis in the absence of any agreed novation – that Motts had made representations to Galliford Try as to the prop forces that could be taken by the concrete slab part of the floor and/or that the steelwork would not be required to perform this function. The judge found there was no representation of this sort by Motts, no reliance by Galliford Try and that Motts had not been negligent.
Switch

This is not a novation in the traditional sense. The "switch" recognises the reality of the design/build situation. The consultant works for his client at the outset and then from a certain stage works for the contractor. The same result could be achieved by bringing to an end the original appointment by the client comprising the services to be performed up to novation, and having a new appointment between the design and build contractor and the consultant comprising the services the consultant is to perform thereafter for the design and build contractor. Under a "switch" form of novation the consultant switches from acting for one client – the original client – to acting for another client – the design and build contractor at the point of novation.

CIC novation agreement

This is a "switch" type of novation. The way the CIC novation agreement achieves this is by the consultant remaining liable to the client in respect of the work done for him prior to the novation. Post-novation, the consultant agrees to work for the contractor and to be liable to him. The contractor agrees to step into the shoes of the original client post-novation and thenceforth act as the client. Thus the "switch" happens at the point of novation.

Under the construction contract the contractor will accept some or all responsibility for design, and this will generally include an element of design done pre-novation (ie, at a time when the consultant was working for the client). The contractor will want a remedy against the consultant who did the design work to cover him in the event that he suffers loss due to an error in that design. The consultant therefore gives a warranty to the contractor in respect of services undertaken pre-novation. He warrants to the contractor that, insofar as the contractor is responsible under the main contract for pre-novation services undertaken by the consultant, such services have been performed for the client in accordance with the terms of the appointment. Then if he has been in breach of the duty owed to his client, and the contractor suffers loss as a result, the contractor will be able to sue him.

An important caveat is included in the CIC agreement: "save that the Consultant shall not be absolved from liability to the Contractor for such loss merely by virtue of that fact that the loss has not been suffered by the Employer". The consultant cannot therefore raise the "no loss" argument, thus allaying a concern that has been expressed about the possible effect of the Blyth & Blyth case.

Services, fees, other changes

The CIC novation agreement allows for the necessary distinction to be made regarding the services, so that the services to be performed by the consultant for the client are properly recorded, and those to be performed for the contractor are similarly properly recorded. If the consultant is, say, inspecting workmanship on behalf of the contractor his obligations will be different from those he would have if he was inspecting on behalf of the client – he will not issue certificates, for example. Similarly, the pre- and post-novation fee can be set out and any other necessary changes to the obligations in the appointment to reflect the fact that the consultant is now acting for the design and build contractor. There is a schedule attached to the CIC novation agreement where the necessary changes in the services and any other obligations can be recorded.

If the consultant agrees to give the client a warranty for work done post-novation, an appropriate form (a supplemental contract) can be found on the CIC's website [at www.cic.org.uk (liability and contracts)].
Conclusion

The CIC novation agreement should be the only one recommended to consultants for the design/build situation. It has been endorsed by all the relevant consultant bodies. This will also mean that the consultants will be engaged on a proper basis and not put into a position of conflict of interest and/or where their duties of confidentiality are broken. Several projects have used this form when the consultants were novated to the design and build contractor.

A final cautionary note: we are already seeing adjudication and claims arising out of novations of consultants to design and build contractors and these will only get worse (i) as time goes on and more projects are carried out on this basis; and (ii) if we are going into a recession when people (particularly contractors) start suing to try and recover the monies they have lost.

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