The Assessment of Change under NEC

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Section 1 Introduction
Introduction

- NEC is a brand name for a family of contracts
- This presentation focuses on the Engineering and Construction Contract (ECC) 3 edition – June 2005
- Similar nature of NEC documents principles will generally be applicable to all NEC contracts
- The assessment of change
  - Time
  - Cost
    - Direct
    - Indirect Costs
NEC Suite of Contracts

» The Engineering and Construction Contract (ECC)
» The Engineering and Construction Subcontract (ECS)
» The Engineering and Construction Short Contract (ECSC)
» The Engineering and Construction Short Subcontract (ECSS)
» The Professional Services Contract (PSC)
» Term Service Contract (TSC)
» Term Service Short Contract (TSSC)
» Supply Contract (SC)
» Short Supply Contract (SSC)
» Framework Contract (FC)
» The Adjudicators Contract (AC)
Section 2 Benefits of the NEC
Benefits of the ECC

» Flexibility

› Multi disciplinary – use in engineering and building work
› Design responsibility can reside in part or whole with either party
› Choice of pricing options – lump sum, target cost, cost plus
› Modular contract form – core clauses, main options and bolt on secondary options
Benefits of the ECC

» Clarity and Simplicity
  › Written in ordinary language, not construction terminology!
  › Simple clause structure; avoids legalistic terminology
  › Subjective decisions minimised
  › Provision of guidance notes and flow charts
Benefits of the ECC

» Provide a stimulus to good management
  › The ECC is a management tool as well as a contract
  › Requires timely and clear decision making process
  › Clear allocation of responsibility
  › Proactive risk management procedures
  › Encourages collaborative working
Section 3 Risk Allocation
Risk Allocation

» One of the key functions of any contract is to allocate risk between the Parties

» ECC does this very effectively and the contract provisions clearly allocate all risks

» ECC has a list of Employer’s risks
  › Sub-clause 60.1 compensation events
  › Sub-clause 80.1 Employer’s risks

» If these events occur the Contractor will be compensated for their effect in respect of time and / or money

» All other risks are the Contractor’s
ECC3 introduced a Risk Register as part of the contract documents. Development of proactive project management ideals. Early identification of risk leading to their elimination / mitigation. Created during the tender process and is a live document updated throughout the life of the project.
Risk Register

» Sub-clause 11.2(14)

› “The Risk Register is a register of the risks which are listed in the Contract Data and the risk which the Project Manager or Contractor has notified as an early warning matter. It includes a description of the risk and description of the actions which are to be taken to avoid or reduce the risk”
Risk Register

» Contract Data is the project specific information
» Contract Data Part 1 completed by the Employer and issued with the tender
» Contract Data Part 2 completed by the Contractor and returned as part of his offer
» Both parts contain the following statement
  › “The following matters will be included in the Risk Register……”
» The consolidated list then forms the initial Risk Register
Risk Register

» Common misconceptions about risk under the ECC
  › Risk is unallocated or that the allocation can be changed by the Risk Register
  › Only risks covered by the contract are those listed in the Risk Register
  › Owner of the risk the person identified in the Risk Register
  › Value of risk allowance is determined by the Risk Register

» Risk Register is in effect for information purposes only

» Should only contain 2 columns
  › Description of the risk
  › Mitigation action
Risk Register

» Review allocation of risk
» “Buying or selling” can be very beneficial
» Any risk transfer has to be captured in the Contract
  › Additional Employer’s risks in the Contract Data
  › Additional Contractor’s risk by amending the contract using a Z clause
Section 4 Early Warnings
Early Warnings

Sub-clause 16 - Early warning

» Contractor or Project Manager gives an early warning as soon as either becomes aware of a matter that may (can be Contractor or Employer risk)
  › increase the total of the Prices
  › delay Completion or delay meeting a Key Date or
  › impair the performance of the works in use
  › increase the Contractor’s total cost
The focus is on resolving and mitigating issues rather than seeking to allocate blame and liability.

While there is still time to positively influence the course of events.

Process is not understood or applied correctly.

Considered as part of the compensation event process – they are NOT!

Failure to raise an early warning will not exclude right to a compensation event.

Notification of an early warning is not notification of compensation event.

Should not be raised for events that have already occurred.

Employer / Project Manager does not raise any.

Issues that affect time, cost, quality not raised & shared if they are not seen as grounds for claim.
Early Warnings

» Sanctions for the Contractor if not given:
  › The compensation event is assessed as if the Contractor had given early warning (Clause 63.5)
  › Disallowed cost if cost was incurred because the Contractor did not give an early warning (Clause 11.2 (25) of Option C, D & E)

» No Employer sanctions
  › Employer will lose the opportunity to mitigate the effects of the early warning
Section 5 Compensation
Events
Compensation Events

» If an event occurs for which the Employer carries the risk the Contractor will be entitled to be compensated for the effect of that event

» Clause 6 of the ECC covers compensation events and contains in a single section the mechanics for notifying, assessing and implementing the effects
  ‣ Time
  ‣ Cost
    – Direct
    – Indirect
    – Disruption

» There is no separate EOT or Claim clauses
Compensation Events

» Strict process to follow with challenging timescales
» Proactive management of change with the intention that the effects of change is assessed and agreed contemporaneously with event arising and preferable before
» Placing the Employer in the lead of the change control process and providing an opportunity to manage and mitigate risk
» Provide certainty and avoid the potential for claims
» Final account not required as each change has already been assessed and agreed prior to Completion or shortly thereafter
Compensation Events

» There are 19 standard grounds for compensation events and a further 7 dependent upon which main and secondary options are selected

1. Project Manager gives and instruction to change the Works Information except
   - a change made in order to accept a Defect
   - a change to the Works Information provided by the Contractor for his design which is made either at his request or to comply with other Works Information provided by the Employer

2. The Employer does not provide access and use of the Site by the later of its access date and the date shown the Accepted Programme

3. The Employer does not provide something which he is to provide by the date shown on the Accepted Programme

4. The Project Manager gives an instruction to stop or not to start any work

5. The Employer or Others do not work within the times shown on the Accepted Programme or do not work within the conditions stated in the Works Information
Compensation Events

(6) The Project Manager or Supervisor does not reply within the period for reply
(7) The Project Manager gives and instruction for dealing with an object of value or of historical or other interest
(8) The Project Manager or Supervisor changes a decision which he has communicated to the Contractor
(9) The Project Manager withholding an acceptance for a reason not stated in this contract
(10) The Supervisor instructs a search for a Defect and no Defect is found
(11) A test or inspection done by the Supervisor causes unnecessary delay
(12) The Contractor encounters “unforeseen” physical conditions
(13) A weather measurement is recorded which is shown to occur on average less frequently than once in 10 years
Compensation Events

(14) An Employers’ risks event occurs – Links to Clause 80.1
(15) The Project Manager certifies take over of a part of the works before both Completion and the Completion Date
(16) The Employer does not provide materials and facilities and samples for test as stated in the Works Information
(17) The Project Manager notifies a correction to an assumption about a compensation events
(18) A breach of contract by the Employer which is not one of the other compensation events under this contract
(19) Prevention, an event occurs which neither party could foresee, can prevent and stops the Contractor completing the works in time or at all
Compensation Events

The procedure follows a logical chain with strict timescales as follows:

- Notification: 8 weeks
- Decision on validity / instruction to quote: 1 week
- Quotation: 3 weeks
- Assessment of quotation / reply: 2 weeks
- Implementation

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Compensation Events

» Notification
  › Either party can notify the other of a potential compensation event
  › If the Project Manager notifies (61.1) you move straight to quotation
  › If the Contractor notifies (61.3) then the Project Manager has to undertake a series of checks to confirm if the notification is a valid compensation event
Compensation Events

» Validity (Cl 61.4)
  › Only the Project Manager can instruct a compensation event
  › Decision within 1 week or a longer period to which the Contractor has agreed
  › If the Project Manager decides that the event notified by the Contractor: -
    — arises through a fault of the Contractor
    — has not happened and is not expected to happen
    — has no effect upon Defined Cost or Completion or meeting a Key Date or
    — is not one of the compensation events stated in this contract
  › The notification is rejected and the matter is closed
Compensation Events

» There is no “independent” Engineer or Contract Administrator

» Appointed by the Employer to “manage the contract for the Employer with the intention of achieving the Employer’s objectives” (ECC Guidance Notes)

» Employed for managerial skills; role not additional to a design appointment

» ECC assumes the Project Manager has the Employer’s authority

» PM is constrained from unreasonable actions under the Contract

» Should act as an impartial certifier (Costain v Bechtel – English Law Case)?

» No right of appeal against a Project Managers decision only recourse is Adjudication or whatever form of dispute resolution identified in the Contract
Compensation Events

» Quotation

› If the Project Manager decides that the Contractor did not give an early warning which an experienced contractor could have given he notifies this decision when he instructs him to submit quotations

› The event is then assessed as if the Contractor had given the early warning

› If the Project Manager decides that the effects of a compensation event are too uncertain he can state an assumption

— The assessment of the compensation event is then based on these assumptions
— If the assumption turns out to be incorrect the Project Manager notifies a correction
— This leads to the award of a new compensation event for the changed effect (60.1(17)

› The Project Manager can enter into discussion with the Contractor about alternative ways of dealing with the event and can ask for alternative quotes (62.1)
Compensation Events

Assessment

› Contractor has only one opportunity to price all the effects of the compensation event

› All compensation events entitle to the Contractor to claim time and money, there are no “neutral events” (CI 62.2)

› 2 principle elements to the assessment
   — Time
   — Cost
     ◦ Direct
     ◦ Indirect
     ◦ Disruption
Compensation Events

Cost

- The changes to the Prices are assessed as the effect of the compensation event upon (63.1)
  - the actual Defined Cost of the work already done
  - the forecast Defined Cost of the work not yet done and
  - the resulting Fee
- The date when the Project Manager instructed or should have instructed the quotations divides the work done from the work not yet done
Compensation Events

Compensation event quotation instructed

Week 1 → Week 2 → Week 3 → Week 4

All forecast Defined Cost
Compensation Events

Compensation event quotation instructed

Week 1 → Week 2 → Week 3 → Week 4

2 weeks actual Defined Cost  2 weeks forecast Defined Cost

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Compensation Events

Week 1 ➔ Week 2 ➔ Week 3 ➔ Week 4

All actual Defined Cost
Compensation Events

Compensation event quotation should have been instructed

Week 1 ➔ Week 2 ➔ Week 3 ➔ Week 4

Compensation event quotation actually instructed

All forecast Defined Cost
Compensation Events

» The drafters have deliberately broken the link between tendered prices and the evaluation of change
» Compensation events are evaluated on the basis of ‘Defined Cost’
» Defined Cost is a defined term that differs between the main options
» The intention is the Contactor should be paid what the events will cost him plus the agreed Fee i.e. he will be compensated
Compensation Events

» Option A & B (and can be used under Option C & D if the Parties agree)
  › Defined Cost is the cost of the components in the Shorter Schedule of Cost Components whether the work is subcontracted or not excluding the cost of preparing quotations for compensation events
  › The Shorter Schedule is in effect a simplified version of the full schedule
Option C & D

- Defined Cost is
  - the amount of payments due to Subcontractors for work which is subcontracted without taking account of amounts deducted for
    - retention
    - payment to the Employer as a result of the Subcontractor failing to meet a Key Date
    - the correction of Defects after Completion
    - payments to Others and
    - the supply of equipment, supplies and services included in the charge for overhead cost within the Working Areas in this contract
  - and
    - the cost of components in the Schedule of Cost Components for other work
  - less any Disallowed Cost
Compensation Events

» Schedule of Cost Components and the Shorter Schedule of Cost Components is split into the following sections

› 1 People
› 2 Equipment
› 3 Plant and Materials
› 4 Charges
› 5 Manufacture and fabrication
› 6 Design
› 7 Insurance

» The schedules are based on actual cost
Compensation Events

» The Fee is applied to the total Defined Cost and is the sum of 2 fee percentages
  › Subcontracted fee percentage – applied to the Defined Cost of subcontracted work
  › Direct fee percentage – applied to the Defined Cost of other work

» Commonly the Contract is amended to provide a single fee percentage

» No definition of what is covered by the Fee in the Contract

» The Contract defines what is in Defined Cost and ALL other cost is deemed to be in the Fee
Compensation Events

» If the effect of the compensation event reduces is to reduce the total Defined Cost then there are far more limited grounds for assessing its effect

» Option A & B
  › A change to the Works Information
  › A correction of an assumption by the Project Manager

» Option C & D
  › A change to the Works Information other than a change to the Works Information provided by the Employer which the Contractor proposed and the Project Manager accepted
  › A correction of an assumption by the Project Manager
Compensation Events

» Time
  › Delay to the Completion Date is assessed as the length of time that planned Completion is later than planned Completion shown on the Accepted Programme (CI 63.3)
» Accepted Programme

› Accepted Programme is the latest programme accepted by the Project Manager
› The latest Accepted Programme supersedes all previous Accepted Programmes
› The programme is at the heart of the ECC contract – joint management tool
› There is an extensive and potentially onerous list of requirements for each programme, however, the level of information required should make it easier to agree the time and cost effects of change
› Float, time risk allowances, statement of how the Contractor plans to do the work identifying principal Equipment / resources etc.
› The programme has to be updated on a regular basis (normally monthly) and submitted for acceptance
› Has to capture all issues that have or will affect progress
› Identify risks and developing mitigating strategies, placing the Employer in control
Compensation Events

Completion Date

Terminal Float

4 weeks

planned Completion
Compensation Events

Compensation event

Completion Date

Terminal Float

4 weeks

planned Completion

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Compensation Events

Compensation event

Completion Date

Terminal Float

2 weeks

2 weeks

2 weeks

planned Completion

2 weeks

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Compensation Events

Compensation event

Completion Date

Terminal Float

4 weeks

planned Completion

4 weeks

2 weeks
Compensation Events

Completion Date

Compensation event

Terminal Delay

4 weeks

planned Completion

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Compensation Events

Compensation event

Completion Date

Terminal Delay

2 weeks

4 weeks

planned Completion
Compensation Events

Compensation event

Completion Date

2 weeks

2 weeks

planned Completion
Compensation Events

Completion Date

Terminal Delay
4 weeks

planned Completion

Compensation event

2 weeks

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Compensation Events

Compensation event

Completion Date

Free Float

2 weeks

planned Completion
Compensation Events

Compensation event

Completion Date

planned Completion
Compensation Events

Compensation event

Completion Date

2 weeks

planned Completion

2 weeks

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Compensation Events

» Disruption
  › If the programme for the remaining work is altered by the compensation event the Contractor includes alterations to the Accepted Programme in his quotation (Cl 62.2)

» Risk
  › Assessment of the effect of a compensation event includes risk allowance for cost and time for matters which have a significant change of occurring and are at the Contractor’s risk under this contract (Cl 63.6)

» Duty of the Contractor to mitigate the effects of a compensation event
  › Assessment are based upon the assumption that the Contractor responds competently and promptly to the compensation event, that any Defined Cost and time due to the event are reasonably incurred and that the Accepted Programme can be changed (Cl 63.7)
Compensation Events

» Acceptance

› The Project Manager can
  — Instruct a revised quotation
  — Accept the quotation
  — Notify that a proposed instruction will not be given
  — Notify that he will be making his own assessment

› If the Project Manager instructs the Contractor to submit a revised quotation he explains the reasons for doing so.

› The Contractor resubmits within 3 weeks

› The Project Manager can extend the time allowed for quotation and Project Managers response if the Project Manager and Contractor agree
The Project Manager can make his own assessment of the effects of a compensation event if (Cl 64.1)

- The Contractor has not submitted a quotation and details of his assessment in the time allowed
- If the Project Manager decides that the Contractor has not assessed the compensation event correctly and he does not request a revised quotation
- If the Contractor fails to submit a programme or alterations to a programme which this contract requires him to submit
- If, when the Contractor submits quotations for a compensation event, the Project Manager has not accepted the Contractor’s latest programme

The assessment made by the Project Manager cannot be challenged or rejected by the Contractor
Compensation Events

» Time Bar
  › 8 week time bar on the Contractor for raising a notification (Cl 61.3)
  › But only from “awareness” of the event

» Default Acceptances
  › Default acceptance of Compensation Event if no response from the Project Manager within the correct timescales (1 week + 2 weeks) (Cl 6.1.4)
  › Default acceptance of quotation if no response from the Project Manager within the correct timescales (2 weeks + 2 weeks) (Cl 62.6)
Section 6 Summary
Summary

» The Assessment of change under the ECC is different to the process under most standard forms of contract

» Designed to support the philosophy of the contract
  › Proactive risk management & early identification of potential problems
  › The contract as a management tool as well as a contract
  › The Employer being placed in charge of the change control process
  › A final account agreed on the last day of the project and not months / years after
  › Provide certainty and avoid the potential for claims
  › Requires timely and clear decision making process
  › Strict process to follow with challenging timescales
  › Team needs to understand the process and have the necessary skills to implement them
10.1 The Employer, the Contractor, the Project Manager and the Supervisor shall act as stated in this contract and in a spirit of mutual trust and co-operation.

Legally enforceable?

His Honour Humphrey Lloyd QC suggest it is (International Construction Law Review, October 2008)

Essential for the benefits of the NEC to be realised

- Application and compliance with procedures
- Early warnings / proactive risk management
- Problem solving
- Sharing on information and issues

If you cannot comply with 10.1 don’t use the NEC!!