NEC3 – not to be left in the drawer

Will Buckby of Beale & Company Solicitors LLP warns that NEC3 users who think it is good enough to leave the contracts in the drawer are missing out on valuable project and risk management tools, as well as heightening the risk of disputes.

KEY POINTS
- Most of the infrastructure sector will be familiar with the NEC3 suite of contracts, which is the most widely used form of contract for infrastructure projects
- The NEC3 forms, particularly the Engineering and Construction Contract (ECC) and the Professional Services Contract (PSC), contain detailed administrative procedures, which act as project and risk management tools
- These procedures include the early warning, compensation event and programme regimes
- Failure to comply with the ECC and PSC can result in contractors and consultants losing out on their entitlements and encourage disputes

Many of us are familiar with the NEC3 suite of contracts. This is most likely because it is the most commonly used standard form of contract to be used in respect of infrastructure projects in the UK. For example, the NEC3 is now used by many local authorities and government entities. It has been used to procure High Speed 1, the London 2012 Olympic Games, Crossrail, and Highways England’s Collaborative Delivery, amongst others. However, many of the NEC3’s users are still not using the contract in the manner it should be used. This is particularly the case for the NEC3 Engineering and Construction Contract (the ECC) and the Professional Services Contract (the PSC), which provide detailed procedures to be operated throughout the project for the benefit of the parties. These procedures are focused on good project management and managing and mitigating risk. Those not using the contract correctly or complying with its terms are at a real risk of losing their entitlements, such as variations (called compensation events), under the relevant NEC3 form. In addition, parties to the contract could be unnecessarily encouraging a dispute. It is widely recognised that one reason (in addition to adjudication) for the limited reported cases on the NEC3 forms is because the risk management procedures therein, where followed, encourage the prevention of disputes. Akenhead J in Atkins Ltd v Secretary of State for Transport [2013] EWHC 139 (TCC) boldly stated that despite the ‘siren or other voices which criticise [the NEC3] for some loose language’ they are ‘highly regarded’ and are seen as ‘providing material support to assist the parties in avoiding disputes and ultimately resolving any disputes that do arise’. It is clear that the NEC3 forms must be read, fully understood and followed by the parties – they should ‘not be left in the drawer’.

The key project and risk management provisions
Act in a spirit of mutual trust and co-operation
The very first provision in the ECC and the PSC is a requirement for the parties to act in ‘a spirit of mutual trust and co-operation’ (sub-cl 10.1 of the ECC and PSC). It is clearly intended to stand out given its prominent place. Much has been written about the meaning of this obligation and to date it has yet to be properly considered by the courts. Keating on NEC3 suggests that this provision lends to a good faith type obligation and one which might require the parties to act in an honest, fair and reasonable manner without improperly exploiting each others’ roles in the contract. If this is correct, this is an obligation which the parties must follow in their day-to-day operation of the project and contract, and suggests the
adoption of a collaborative or ‘friendly’ approach. This should, of course, mitigate the potential of disputes arising. However, this provision is ambiguous – what does ‘a spirit of mutual trust and co-operation’ actually mean? Further, as noted above, the wording has yet to be properly tested by the courts and in recent decisions (such as Mears Ltd v Shoreline Housing Partnership Ltd [2015] EWHC 1396), where the wording was ‘considered’, it was held that, in any event, a duty of mutual trust and co-operation will not override an existing contractual obligation. This will most likely limit the application of this clause.

Early warning notices and risk reduction meetings

The requirement for early warning notices and risk reduction meetings are at the heart of the ECC and PSC and are key project and risk management requirements. The contractor and project manager in the ECC, and the employer and the consultant in the PSC, must give an early warning to each other as soon as either becomes aware of any matter which could, amongst other things, increase the total of the prices, delay completion, and delay meeting a key date. Additionally, the contractor/consultant must provide an early warning notice of any matter which could increase the employer’s total cost (sub-cl 16.1 of the ECC and sub-cl 15.1 of the PSC).

An early warning notice kick starts a process. Following an early warning notice, the project manager in the ECC and the employer in the PSC is then required to enter the early warning matters into a risk register. Thereafter, either party to the relevant NEC3 form may instruct the other to attend a risk reduction meeting in order to discuss how to mitigate and avoid the risks identified in the early warning notices (sub-cl 16.2 of the ECC and sub-cl 15.2 of the PSC). The risk register is then updated to record the agreed actions (sub-cl 16.4 of the ECC and sub-cl 15.4 of the PSC).

It is important to stress how widely couched the obligation to give an early warning notice really is. The warning has to be given as soon as there is awareness of a matter which could (and not ‘will’) cause one of the circumstances set out in sub-cl 16.1 of the ECC and sub-cl 15.1 of the PSC to arise. This is likely to lead to a variety of early warning notices given on any project. Individuals administering the NEC3 forms should not underestimate this obligation.

Moreover, the consequence of failing to give an early warning notice is potentially significant. If the project manager in the ECC or the employer in the PSC decides that the contractor/consultant did not give an early warning of an event which an experienced contractor/consultant could have given, in assessing a variation, the contractor/consultant will not be entitled to additional money or time which could have been mitigated by either party by the early warning procedure (sub-cl 61.5 of the ECC and PSC). Accordingly, this could limit a contractor or consultant’s entitlement in the event that a compensation event arises.

This early warning procedure does mitigate disputes arising and, as noted above, is at the heart of the NEC3 form. If not correctly followed, it can result in the contractor/consultant not being entitled to compensation. Contractors and consultant must be, and are not always, alive to the regime. In addition, this regime suggests an administratively demanding procedure which is not included in many other standard form contracts and which does require additional project management type resource throughout the course of the project. Contractors/consultants, and particularly those who are not geared up to operating the NEC3 procedures, will need to ensure that they are prepared and perhaps have priced the additional time and manpower required.

Variations – compensation events

The ECC and PSC contain a detailed variation procedure, which must be followed in order for the contractor/consultant to avoid missing out on its entitlement to a compensation event. Additionally, the ECC and PSC require compensation events to be dealt with as and when they arise so that the compensation event can be managed accordingly, and importantly not left to a later date, such as at the end of the project, when it is more likely that a disagreement might arise.

Sub-clause 60.1 of the ECC and PSC provides a long list of ‘compensation events’, which if arise, trigger a reassessment of the prices, key dates and completion date. These include, for example, in the ECC, instructions from the project manager changing the works information (sub-cl 60.1(1)) and events which neither party could prevent and which is so unlikely that it would be unreasonable to expect an experienced contractor to have allowed for (sub-cl 60.1(19)). There are many more and a similar, but certainly not identical, list is provided in the PSC.

Perhaps the most significant provision in the compensation event regime is sub-cl 61.3 of the ECC and PSC, which provides a strict timescale in which the contractor/consultant must notify a compensation event. It provides that the contractor/
consultant must notify ‘an event which has happened or which he expects to happen’, and which he believes is a compensation event, within eight weeks of the contractor/consultant becoming aware of the event; if the contractor/consultant does not, it will not be entitled to additional fees and an extension of time. There is one exception to this – where an event arises from the project manager/employer giving an instruction, changing an earlier decision or correcting an assumption. However, it means that in certain circumstances, a failure by the contractor/consultant to notify a compensation event in accordance with sub-cl 61.3 may operate as a time bar to the contractor/consultant’s entitlement. Accordingly, it is vital that the contractor/consultant is aware of this provision and manages it accordingly.

The compensation event provisions which follow set out the procedure for assessing and implementing compensation events. These too contain timescales which need to be followed, particularly in relation to compensation event quotations (the contractor/consultant is required to provide one within two weeks of being instructed to do so (sub-cl 62.3 of the ECC and PSC)) and revised compensation event quotations (within three weeks of being instructed (sub-cl 62.4)). It goes without saying that it is vital that the compensation event regime in the ECC/PSC is complied with in order for the contractor/consultant to receive its entitlement to additional fees and/or an extension of time. Unfortunately, this is not always the case and is a factor which leads to contractors/consultants missing out on a compensation event and increases the potential for disputes to arise.

Programme
Unlike other standard forms in this sector, at the heart of the ECC and PSC is a detailed mechanism relating to a programme. The contractor/consultant is required to regularly update and agree with the project manager in the ECC, and the employer in the PSC, a detailed programme. This too is a project and risk management tool, as the obvious benefit of doing this is that there are never any surprises in relation to the order and timing of operations and completion, for example. Further, the ECC and PSC require the programme to specifically deal with certain risk items including float, time risk allowances and health and safety requirements, with a view to further mitigating the potential for a dispute.

Usually a programme is included in the ECC or the PSC, and if one is not, the ECC and PSC require the contractor/consultant to submit its first programme to the project manager in the ECC and the employer in the PSC, for acceptance in a defined timescale (sub-cl 31.1 in the ECC and PSC). Thereafter, revised programmes are required to be submitted when (i) the project manager/employer instructs the contractor/consultant to; (ii) when the contractor/consultant chooses to; and (iii) in any event no longer than the intervals as stated in the ECC/PSC which is usually monthly (sub-cl 32.2 of the ECC and PSC). Further, revised programmes will be required if the project manager/employer rejects a programme, and it can do so if the plans included therein are not practicable or unrealistic, or the programme does not comply with the detailed requirements provided in the ECC/PSC (sub-cl 31.3 of the ECC and PSC). In addition to this detailed regime, the list of items to be included in each programme is substantial – there are 17 different requirements. As well as the items mentioned above, there is even a requirement for the contractor/consultant for each operation to provide:

‘... a statement of how the [contractor/consultant] plans to do the work identifying the ... resources which he plans to use and other information which the [Works Information/Scope] requires the [contractor/consultant] to show on a programme’.

This whole programme requirement is a big undertaking, along with the other additional administrative procedures in the ECC and PSC.

The programme clearly serves as a project and risk management tool, although the programme regime, just like the early warning and compensation procedure, will require additional resource to manage the process.

Conclusion
The NEC3 forms, particularly the ECC and PSC, contain some administratively demanding procedures, which contractors and consultants may not be accustomed to in other forms. Whilst the NEC3 suite is widely used, particularly in the infrastructure sector, there is often non-compliance with these procedures, which means that contractors and consultants are not always obtaining their entitlements under the ECC and PSC and disputes are not always mitigated. It is important for parties to the NEC3 forms to understand these procedures and to act in accordance with the contract. The NEC3 forms are not contracts to be left in the drawer, but are project and risk management tools to assist delivery of the project.  

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