NEC4 increases consultants’ risk

Will Buckby and Andrew Croft of Beale & Company Solicitors LLP examine the new NEC4 Professional Services Contract and find the changes from the previous contract to be more than simply an evolution. Consultants face increased potential risk, they warn.

KEY POINTS
- The changes from the NEC3 PSC are more than just an ‘evolution’
- The general structure of the NEC4 PSC is similar to the NEC3, and there are limited amendments to the key provisions
- NEC4 still requires parties to be proactive in managing the contract so it should not be ‘left in the drawer’
- Significant changes include introduction of the service manager role and the use of defined costs and disallowed costs, as well as key changes to the payment process and the approach to liability
- The consultant’s potential risk on a project is increased
- Positive changes include a new Option Clause X10 in relation to Building Information Modelling

The NEC4 suite of contracts was published on 22 June 2017. The changes to the NEC3 forms are described by the NEC as ‘evolution not revolution’ and include a number of new features and some new forms of contract, as a result of industry feedback (such as an design build and operate form and a consultation version of an alliancing contract).

There has been a considerable amount of commentary on the Engineering and Construction Contract (ECC) but very little has been published on the Professional Services Contract (PSC).

General structure
The structure of the NEC4 PSC is very similar to that of the NEC3 PSC. For example, there have been very limited amendments to the duty to act in the spirit of mutual trust and cooperation (cl 10.1) and to the early warning notice and compensation regimes (including the condition precedent to notifying compensation events) (sub-cll 15 and core cl 6).

These are key parts of the PSC which require the parties to be proactive in managing the contract throughout a project and support the NEC’s aim of good project management. For this reason, as with the NEC3 PSC, the NEC4 PSC still should not be ‘left in the drawer’.

In addition, the duty of care is unchanged. The Consultant’s obligation is to use ‘the skill and care normally used by professionals providing services similar to the service’. This probably still means ‘reasonable skill and care’ but ideally should have been clarified.

Significant changes
There are some significant changes in the NEC4 PSC, which in our view mean that the NEC4 PSC goes much further than a simple ‘evolution’ of the NEC3 form.

These changes include: (1) the new role of the service manager; (2) the use of defined cost and disallowed cost; (3) amendments to the payment process; (4) a new approach to liability; and (5) the new Secondary Option X10 in relation to building information modelling (BIM).

Service manager
The service manager is a new key role under the NEC4 PSC and is similar to the role of the project manager under the NEC3 ECC.

The service manager is required to act in a spirit of mutual trust and co-operation, gives notices and instructions under the contract, accepts programmes and assesses payment and compensation events,
amongst other things. Whilst it is common for a construction contract to be administered by a third party, such an approach is extremely rare for professional services agreements. It will therefore introduce additional complexity and certainly cost to the NEC4 PSC and will need to be managed carefully.

**Defined cost and disallowed cost**

The NEC4 also takes a different approach to valuing sums due to the consultant.

Under the NEC3 PSC Secondary Options C (target cost) and E (time based contract), the consultant was paid on a ‘Time Charge’ basis, by reference to hourly rates. Under the NEC4 PSC, payment under Options C and E (now ‘costs reimbursable’) is on a ‘defined costs’ basis. The consultant is paid defined costs plus a fee percentage and defined costs are used to assess compensation events under all options.

This approach has caused some concern for consultants. One reason for this is that, under Options C and E, disallowed costs are deducted from defined costs when assessing payment. Disallowed costs are often used under the ECC to reduce the contractor’s entitlement to payment, and this approach could also be adopted by the service manager under the NEC4 PSC. Clients could also seek to amend the PSC to widen the scope of disallowed cost, which should be resisted.

Another concern with this approach is that under Options C and E, defined costs is determined using the schedule of costs components. The schedule of cost components entitles the consultant to the costs of (1) people directly employed to provide the service, (2) sub-contractors; and (3) the overhead percentage of the costs of the consultant’s employees. To show the costs of its employees, the consultant must:

- divide the total of payments made to the employee by the total time recorded; and
- multiply that sum by the time recorded for work on the contract.

This will involve taking into account specific details of the employees’ employment contract, including for example, salary, pensions and insurance and will be a challenging administrative burden.

In addition, any failure to justify costs will make them a disallowed cost, which means the consultant will need to keep evidence of how they have calculated the cost of their employees and provide this information to the service manager. Consultants’ businesses are not set up to be able to easily provide this much detail to demonstrate their entitlement to payment so this is a challenge.

Moreover, the information required to calculate employee costs will be confidential between the employee and the consultant and will also include personal data, the processing of which is limited by the *Data Protection Act 1998*. Care will therefore need to be taken when providing supporting information under the NEC4 PSC.

**Payment regime**

The payment regime under the NEC4 PSC has also changed substantially and is a lot more administrative.

Under the NEC3 PSC, the consultant simply submitted an invoice, which was the payment notice under the *Housing Grants, Construction and Regeneration Act 1996* (the *HGCRA 1996*). The due date was the date of the invoice and the final date for payment was 21 days after the invoice was submitted.

Under the NEC4 PSC, the consultant is required to submit an application for payment before the assessment date. The service manager then certifies payment within one week of the assessment date, with the service manager’s certificate being the payment notice under the *HGCRA 1996*. However, that is not the end of the process. The consultant must then also submit an invoice within one week of the service manager’s certificate in order to be paid. The final payment date for payment is now the later of 14 days from the application date and 7 days from submission of an invoice, so failure to submit an invoice will delay payment. This is much more administrative than payment under the NEC3 PSC and will need to be managed carefully. In particular, the process gives the service manager two ‘bites of the cherry’ to pay the consultant ‘less’, through the certificate and a pay less notice. This is not ideal.

**Liability**

The liability position under the NEC4 PSC has also changed significantly.

The consultant’s liability under the NEC3 PSC was limited to the amount stated in the contract data Pt One, other than for excluded matters. This has not changed. Further, under the NEC3 PSC the consultant indemnified the employer against claims as a result of an infringement by the consultant of the rights of Others’ (eg intellectual property claims).

Under the NEC4 PSC, the scope of the consultant’s liability is much more complex and wider. First, the
The consultant must pay to the employer any costs as a result of a consultant liability (sub-cl 82.1). The consultant’s liabilities in sub-cl 81.1 unsurprisingly include costs incurred as a result of the consultant’s failure to exercise the required skill and care and costs related to and death or personal injury to the consultant’s employees. Most would agree that this is acceptable. However, the consultant’s liabilities also include claims from and compensation payable to third parties as a result of the consultant providing the service (ie doing all work necessary to complete the services in accordance with the contract).

The consultant’s liabilities do not include the matters stated as being client liabilities in cl 80.1. The client liabilities include claims from third parties due to an unavoidable result of the providing the service and a fault of the client, its employees or any person contracted to it, and any additional liabilities in the contract data.

The consultant’s liability will therefore be difficult to unravel in the event of any claim.

Additionally, the NEC4 PSC does not include sub-cl 82.2 of the NEC3 PSC, which was a shortened net contribution clause. Instead, the client’s right to recover costs as a result of a consultant liability is reduced to the extent that an event for which the client is liable contributed to those costs. This has a more limited effect than sub-cl 82.2. For example, if the costs are jointly caused by a subcontractor or a member of the public it will have no effect.

This liability position is very complex and, amongst other things, means that the consultant could be liable even though the consultant has complied with the contract. This is a significant risk. The consultant also takes a number of third party risks arising from the contract (which could include for example liability under any third party agreements the client enters into). As liability can arise even though the consultant has not been negligent or in breach of contract, this is likely to be inconsistent with most professional indemnity insurance arrangements.

On the other hand, the NEC4 PSC does include some additional protection to the consultant’s liability; sub-cl 20.3 limits the consultant’s liability for defects to where it has failed to exercise the required level of skill and care.

Nevertheless, as a result of the new approach to consultant liabilities, the NEC4 PSC exposes the consultant to wider liability than the NEC3 which is a real concern.

**BIM**

The NEC4 PSC (and ECC) includes a new Option Clause X10 (BIM). This is a positive step; it is the first attempt in a standard contract suite to properly address BIM other than referring to any ‘BIM Protocol’.

Option X10 refers to two main documents; the information executive plan and the information model requirements, which ties in with the two key documents required under PAS 1192-2, the BIM execution plan and the employer’s information requirements.

If Option X10 is used, the information model and rights in any information used to create or change the information model will be owned by the client unless the information model requirements say otherwise. This is a commercial risk for the consultant.

In addition, this position potentially conflicts with Option X9 (transfer of rights). Ownership of the rights in the consultant’s documents will only transfer to the client under the PSC if Option X9 applies. Option X10 (if used without Option X9) could therefore result in the ownership of the BIM related information transferring to the client whilst intellectual property rights other documents are retained.

**Conclusion**

A number of the changes which have been made to the NEC4 suite and to the PSC are a positive step (such as the new BIM Secondary Option X10) and as commented above, the fundamental principles of the NEC3 PSC remain.

However, the amendments to the NEC4 PSC go much further than the NEC suggests in describing the changes as ‘Evolutionary not Revolutionary’ and have more significant consequences than the changes to the ECC. In particular, under the NEC4 PSC the consultant’s rights depend upon the role of a new third party, the service manager, the consultant’s entitlement to payment does not reflect consultants’ business models and the payment process is much more administrative. In addition, the scope of the consultant’s liability has increased and is complex, and the new Secondary Option X10 means that the consultant may be required to sacrifice intellectual property.

Consultants should therefore review the NEC4 PSC carefully before entering into it and consider requesting amendments, particularly in relation to liability. **CL**