However, performance damages are notoriously hard to apply as the contractor can often come up with reasons why they do not apply, such as things the client has or has not done that prevented the project reaching the required level of performance. This is a good reason to not use them as, if they are specified, they can become the focus if a problem occurs. Consequently, rather than protecting the client from poor performance, they may well encourage it.

It is far better to cap a contractor's downside by using option X18, limitation of liability. While not having X17 on low performance damages will make it harder for a client to recover damages, it reduces the focus on them. This allows

- less risk allowance in a contractor's prices
- participants to focus on achieving superior performance.

Incentivising with NEC3 bonuses

The most obvious ECC bonus to use is option X6, bonus for early completion, where the contractor is paid a bonus for each day that completion or take over occurs ahead of the contractual completion date.

As with option X7 on delay damages, X6 can apply to sections of the works. Note that if meeting a specific date is especially important to a client and it is willing to pay a 'drop dead' bonus, then the wording here is not applicable.

In addition, option X20 on key performance indicators can be used, whereby targets are specified in an incentive schedule. These can be interim targets – which 'indicate' that the contract is on or ahead of expected performance – or end contract targets, in which case they are not 'indicators' but results.

Summary

Using NEC3 secondary options to stimulate improved contractor performance is not hard: the wording is already there. What does require thought and dialogue by clients is

- being clear about what is important to the client (the objectives) and why
- deciding how objectives will be measured and what targets will be set
- using a combination of positive (bonuses) and negative (damages) incentives, but with a greater emphasis on the positive
- constructing an incentive plan that both reflects the value the client puts on achievement of each objective with the costs (and hence profit) the contractor will incur in delivering them – otherwise the contractor will be over- or under-incentivised for each objective in respect of the value the client puts on each.

The key is simplicity, so clients should focus on the few key objectives that are important to them rather than trying to incentivise everything. Lastly, never forget that the biggest incentive of all is repeat order profitable work.

Reference

1. Broome, J. *Procurement routes for partnering: a practical guide*, Thomas Telford, 2002, chapter 5, available online at www.icevirtuallibrary.com or free from the author.

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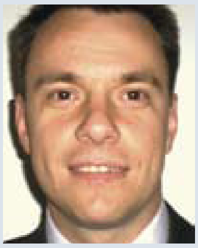
Programming non-implemented compensation events



GLENN HIDE NEC CONSULTANT

It is not uncommon for people to take a literal, isolated meaning of the second bullet point of clause 32.1 of the NEC3 Engineering and Construction Contract (ECC), which states that a revised programme should, 'show the effects of implemented compensation events'. Their response has been not to show 'non-implemented' compensation events, even though these can have a major impact on the programme.

The situation was perhaps further clouded by the June 2006 amendment to clause 32.1, which removed a requirement to include the effects of notified early warning matters in revised programmes. My article in Issue 39[1] dealt specifically with early warning matters – which should not simply be ignored by the programme – while this article considers what to do with compensation events prior to implementation.

Programme must show true picture

The other bullet points in ECC clause 32.1 remind users that the revised effect of all programme activities has to be shown on each revised programme. One of the prime functions of the programme is to show the true picture of the remaining works to be executed, and the contractor's planned completion date in relation to the completion date at that point in time.

It is also clear under ECC that a compensation event only becomes implemented when the time and cost effects have been agreed, the project manager has made a final assessment, or the quotation has been deemed accepted. As a result, in certain circumstances it is possible for the work to have been completed on site but the cost has not yet been agreed.

While the contractor may feel it has 'implemented' the work, contractually it has not.

Example of non-implemented event

Say a contractor installing some pipework finds a high voltage cable in the way of the pipe route. This is notified to the contractor as a compensation event by the project manager, and plans are put in place by the employer to have the cable rerouted with the relevant electricity company. This will delay the pipework by 2 weeks and, other than doing some preparatory work the other side of the cable, works largely cease on this activity. The activity happens to be on the critical path so despite, some mitigation measures by the contractor, the event will be affecting planned completion and thus completion date.

The normal compensation event process for quotation and assessment is rarely a quick or smooth process. It is highly likely that the compensation event will take 5–6 weeks to agree the quotation between the parties – and, practically speaking, very often significantly longer. Only when a quote is accepted or the project manager has assessed it directly will the event be 'implemented' under the contract.

It is frankly ridiculous therefore for anyone to think that the event should not be shown on a programme in the belief that it only needs to be shown it when it becomes implemented. The event is affecting the programmed works and changing the sequence and resource pattern that the contractor is executing. In this instance the critical path is also being delayed by the event, which has yet to have its cost agreed.

Therefore, if the event is not shown on the latest programme issued for acceptance, the programme would not be realistic or practicable – and indeed would be a reason for non-acceptance of the programme under clause 31.3.

Reflect all activities in programme

Any programme should be a real management tool that reflects all of the project programme activities and their relative effects upon each other. As soon as a compensation event is notified and a quotation requested under clause 61.1, it will more often than not be affecting the remaining works in some way and should therefore appear on the programme.

Early on in the process it may not be clear the extent of the impact or duration that this additional activity will have but, for each programme that is produced, the contractor should simply update that activity with the information it knows at that point.

The simple approach is for the contractor to show the minimum impact that it knows the activity will have at this point in time. This way the contractor is not putting in too many activities that could otherwise be artificially pushing out the planned completion date, only to come back at a later date as the activity does not have as bad an impact as envisaged.

The minimum periods for a given activity can be agreed by both parties, and even formalised as project manager's assumptions under clause 61.6, whereby the project manager confirms what assumptions to make for the purpose of the quotation and resultant programme.

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FAQs

ROBERT GERRARD NEC USERS' GROUP SECRETARY

This is a selection of recent questions to the NEC Users' Group helpline and answers given. In all cases it is assumed there are no amendments that materially affect the standard NEC3 contract referred to.

Spares in supply contracts

Question

How do I deal with the provision of spares in the NEC3 Supply Contract (SC)?

Answer

Any spares and replacement parts for the goods which the purchaser requires the supplier to provide should be stated in the goods information. The SC does not include for the supplier to provide spares after the last defects date. Unless they are very small amounts on money to provide such spares, they would usually be itemised on the price schedule.

Incoterms

Question

Can I use the SC in conjunction with the International Chamber of Commerce's Incoterms?

Answer

The SC requires the purchaser to prescribe its supply requirements separately within the documentation to ensure such matters are dealt with clearly. Users may, if necessary, make use of Incoterms 2000 (or Incoterms 2010, due to enter force on 1 January 2011) to do this.

The Incoterms are the internationally accepted official rules for the interpretation of trade terms that are most commonly used in international trade. Such terms are designed to overcome the uncertainties of different interpretations of trading terms in different countries. They are not a contract in themselves and only cover some of the obligations required by a supply contract.

For domestic procurement or international procurement within common trading areas, users may prefer to make their own arrangements in the supply requirements as they are unlikely to involve freight forwarding agents and customs barriers. In this situation, Incoterms could at least be used as a guide for consideration by the parties

Revising compensation event quotations

Question

We are using the NEC3 Engineering and Construction Contract (ECC). Is a contractor allowed to revise a compensation event quotation after the 3 week deadline if they have missed something? Also, if they have been asked to substantiate a cost for something and in doing so realise they have made an error with a quantity in the quotation, are they entitled to change it after the 3 week deadline?

Answer

If the contractor has not submitted a quotation for a compensation event within the 3 week deadline, then the default falls to the project manager to assess under ECC clause 64.1. The project manager assesses this as if he or she were the contractor, using the exactly the same provisions of the contract, and have the same period of 3 weeks that the contractor had.

If the project manager had received the quotation and asked for further information (as provided for in clause 13.4), then strictly this all needs to be done within the 3 weeks, unless both the project manager and contractor agreed to the extension before the submission is due. An alternative is to reply within 2 weeks of receiving the submission, then ask for a revised quotation, the revisions possibly not relating to time or money but instead to details.

Whichever of the routes is taken, if an error in quantities in the quotation becomes apparent, then this should be corrected by either the contractor when submitting a revised quotation, or by the project manager if he or she decides not to instruct the submission of a revised quotation but to assess it directly (due to one of the clause 64.1 reasons).

Either way, I do not see anywhere in ECC that says the contractor stands by an arithmetical or other error if it is spotted before implementation and all other timescales are adhered to.

Completing agreement documents

Question

Consultants have prepared a contract using the ECC option B (priced contract with bill of quantities). In order to wrap the contract documents up, ready for sealing, our legal department demands that an original ECC contract itself is handwritten upon as being the basis of the contract. They do not just want the details written in the tender documents just to be signed by the parties. Can you tell me if there is actual need to enter details in a printed NEC3 form? I am confused here as the contract data states, 'completion of the data in full…is essential to create a complete contract'. So I do not see why we would not formally complete an actual ECC contract as part of the final contract.

Answer

ECC is a standard form of contract that is not itself completed (i.e. it is not necessary to write upon). Instead it is referred to and therefore implied into the contract (executed on the form of agreement). Historically, for other forms of contract, some parties have bought a new contract and handwritten the entries required so that it is a nice, neat contract duly executed.

ECC is different as it is effectively six contracts in one and has an array of secondary options available to choose from. It is basically a shopping list of available clauses. You make your choice of the main and secondary options in contract data part one and that effectively forms the terms and conditions for the contract. In turn, the form of agreement refers to the contract data part one and the contract is concluded.

For completeness of the entire contract package, you could include an unmarked ECC with the bundle, but it is not necessary. It could be possible to write on the contract data part one within an unmarked ECC but I do not see the point of this as it can better and more accurately be prepared on the templates available for the contract data.

The note in the contract data about completing it in full is a note to the document compilers when preparing the contract data to make sure they properly complete this document at tender stage.

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If planning approval for a compensation event will be, say, a minimum 3 weeks but could be 6 weeks, the programme should show 3 weeks for now as it will definitely have that effect, and show any further delay as and when that becomes apparent. Any further delay will be reflected in future programmes, but in the meantime it is showing what is known now as to the effects on the project. In the example above with the cable, the event – whatever it is called – is affecting the programmed works and should be reflected accordingly in the latest programme for acceptance.

Summary

All notified compensation events that are affecting remaining works should be shown as soon as the minimum known affects can be ascertained. Contractors should not wait for the event to become 'implemented' before it appears on a programme issued for acceptance.

The ongoing effects of the event, along with every other programme activity, will be regularly updated and reflected in subsequent programme submissions.

Reference

1. Hide, G. Programme effects of early warnings, *NEC Users' Group Newsletter*, 39, July 2007, p5.

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