

NEC3 to NEC4 : the **good**, the **bad** & the **ugly** (or why aren't you using NEC4 ?)

Jon Broome
BEng PhD FAPM
leading | edge
projects consulting ltd

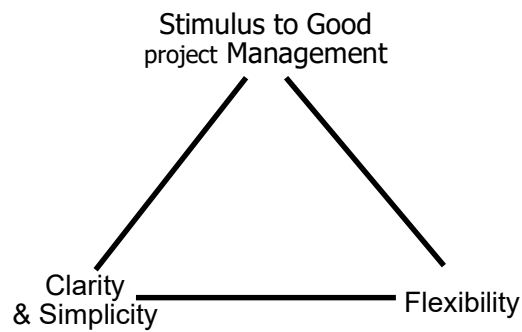
1

Objectives & Agenda

- ❖ To highlight the key changes that have been made.
- ❖ To express an opinion on what is **good** (most of the changes), **bad** (really 'could do better') & **ugly** (the few clangers they dropped).
- ❖ First 5 minutes : this slide & big picture
- ❖ Next 10 minutes : the contract strategy changes e.g. new members of the family, main & secondary options, including dispute clauses.
- ❖ Final 10 minutes : changes to the ECC (Engineering & Construction Contract) with attention on the payment, programme, early warning & compensation event clauses + a mention of the Schedule of Cost Components.
- ❖ Questions

2

NEC's 3 original objectives



Objectives for the 4th edition

- ❖ inspire increased use of NEC in new markets and sectors.
- ❖ support new approaches to procurement which improve contract management.
- ❖ provide greater stimulus to good project management.
- ❖ but **not** 'collaboration' !

Two changes in terminology

These apply across the family :

- ❖ '*Employer*' becomes '*Client*' as more commonly accepted across sectors
- ❖ Works / Service / Goods Information all become 'Scope' : avoids need for generic statements when subcontracting.

Both are '**GOOD**' changes.

The NEC4 family of contracts :

- ❖ **Engineering and Construction Contract (ECC)**
- ❖ **Engineering and Construction Subcontract (ECS)**
- ❖ **Engineering and Construction Short Contract (ECSC)**
- ❖ **Engineering and Construction Short Subcontract (ECSS)**
- ❖ **Professional Service Contract (PSC)**
- ❖ **Professional Service Short Contract (PSSC)**
- ❖ **Professional Service Subcontract (PSS) - NEW**
- ❖ **Term Service Contract (TSC)**
- ❖ **Term Service Short Contract (TSSC)**
- ❖ **Term Service Subcontract (TSS) - NEW**
- ❖ **Design, Build and Operate Contract (DBOC) - NEW**
- ❖ **Supply Contract (SC)**
- ❖ **Supply Short Contract (SSC)**
- ❖ **Dispute Resolution Service Contract (DSRC) - NEWLY NAMED**
- ❖ **Framework Contract (FC) and**
- ❖ **Alliancing Contract (ALC) – NEW, but recently re-launched.**

Changes to the Family

- ❖ The **GOOD** : Two new subcontracts – the **PSS** and **TSS** – as reduces the need to amend main contracts.
- ❖ The **Could do Better** : Subcontracts for compatible short versions of these contracts.
- ❖ The **GOOD** : the **DBO** contract as :
 - saves having to have an extra over-arching agreement which ties **D**, **B** & **O** together.
 - encourages use of a Finance+**DBO** contract

Changes to the main payment options

- ❖ **Professional Service Contract (PSC)** has lost '**option G : Term Contract**'.
- ❖ Often a *Client* wants a consultant to provide a base level of service for a period of time, with the ability to instruct additional Tasks for minor projects as & when required without having to put new contract in place.
- ❖ NEC publishers say use **Term Service Contract (TSC)**, but you need an Affected Property, insurance is different etc. so would need to do multitude of tweaks.
- ❖ Far easier to update & upgrade **NEC3 PSC** Option G to be compatible with **NEC4 PSC**.

Changes to the 'W' Dispute options

- ❖ W1 and W2 are in NEC3 and for Adjudication. W2 is for the UK and W1 for the rest of the world.
- ❖ In NEC4, both options now have *Senior Representatives* before you get to Adjudication. In W1 it is mandatory, whereas in W2 it can't be and isn't.
- ❖ New to NEC4, is W3 : The Dispute Avoidance Board
 - who are 1 or 3 experienced people who keep in touch with the contract;
 - if a potential dispute arises, they try to help resolve it, then make recommendation;
 - Parties have to refer a dispute to it before going onto adjudication, so is not compliant with Construction Acts.

BUT could have easily tweaked it, as W4, to be UK compliant.

Changes to the 'X' Clauses.

- ❖ **'X8 : Undertakings to the Client or Others'** : Previously no X8 in **ECC**, but 'Collateral Warranties' in **PSC**. I like that :
 - broadens scope of what is covered i.e. not just CW's
 - is now in **ECC** and **TSC**, but not **Supply Contract**.
- ❖ New **'X9 : Transfer of rights'** in **ECC** for material developed for contract as per NEC3 **PSC**.
- ❖ New **'X10 : Information Modelling'** replaces 'Employer's Agent' in NEC3 **PSC** as :
 - NEC4 **PSC** now has a *Service Manager*.
 - allows for broader application than BIM
 - BIM Protocol v1 was a contractual car crash waiting to happen & NEC3 Guidance Notes on BIM were vapid.

Changed 'X15 : *Contractor's design*'

- ❖ **ECC** always allowed for any extent of *Contractor* design, **but** previous X15 only limited *Contractor's* liability down to 'reasonable skill and care' and correction of Defects .
- ❖ New X15 does above *and*
 - covers Professional Indemnity insurance
 - changes wording to that which insurance industry comfortable with
 - changes burden of proof onto *Client*
 - covers Intellectual Property (IP) ownership of material
 - has a *period for retention* of material**but** does not sufficiently cover Background IP in design.
- ❖ Not initially, but January 2023 updates to **ECSC** & **ECSS** included words to allow for simple *Contractor* design.
e.g. where patented systems used or attic conversations.

Changes to the 'X' Clauses.

- ❖ Inclusion of '**X22 : Early Contractor Involvement**' and '**Y(UK)1 : Project Bank Account**' from consultative documents / separate addendums. X22 has since been amended in every update.
- ❖ New '**X21 : Whole life cost**' where *Contractor* may propose an idea which reduces wlc and gets a share of wlc savings *but* would like to have
 - seen proportions stated in Contract Data,
 - whole life **value** (benefit/wlc) clause
 - what happens if *PM/Client* steals 'similar' idea ?

Changes to the 'X' Clauses.

- ❖ No change to '**X1 : Price adjustment for inflation**', so does not cover inflation to tendered Defined Costs.
- ❖ '**X4 : Ultimate Holding Company Guarantee**' has changed from 'Parent Company Guarantee'. The UHC could be an offshore hard to get to company. Better to have one you can get to. I.e. UK or Ireland-based.
- ❖ '**X18 : Limitation of Liability**' still contains a 'total liability' cap which has four types of damages or negative incentives as 'excluded matters'. So not really a 'total liability' !

New X29 Climate Change clauses

- ❖ Published April '22
- ❖ An empty vessel:
 - it describes process and incentivisation for environmental matters, but
 - leaves the content to be filled up by the *Client*.
- ❖ I have mixed emotions about it
 - promotes environmental consideration, but
 - not social value
 - everything it promotes can already be done without it. Depending on circumstances, it would complicate the contract if used.

Some other changes across the family

- ❖ Adding of 'boilerplate' clauses wrt to Corrupt Acts – see **ECC** clauses 11.2 (5) and 18.
- ❖ Tidying up of Subcontractor definition to exclude labour only / agency staff & hire of Equipment – see **ECC** clause 11.2(19)
- ❖ the prod to use cloud-based NEC communication systems as almost hard-wire in contractually compliant responses and make it evident who is operating the contract & who is not – see **ECC** clause 13.2

Some other changes across the family

- ❖ that, when not accepting a communication, the *Project Manager* or equivalent has to not just state contractual reason for not accepting, but also give "sufficient detail to enable the *Contractor* to correct the matter" - see **ECC** clause 13.4
- ❖ greater emphasis on *Contractor* putting forward proposals. I.e.
 - value engineering of *Client* Scope as core clause 16 for all options with the 'value engineering percentage', under options A & B, being the *Client's* share based on forecasts; and
 - acceleration under clause 36;
 - whole life costs under X21.

Some other changes across the family

- ❖ NEC4 Section 8 is now 'Liabilities and Insurance' vs 'Risks and Insurance'.
- ❖ **Not so sure** about listing out "Client's liabilities" and then "Contractor's liabilities". What happens if an event is in neither or could be in both ?
- ❖ A Schedule of Cost Components for all 'long' forms, although have reservations for calculating People costs under **PSC**
- ❖ Schedule now includes Subcontractor costs.
- ❖ One *fee percentage* applied to Defined Costs.

Payment (1½)

- ❖ New clause 50.2 makes it mandatory for the *Contractor* to submit an application before each assessment date, with details and "in the form stated in the Scope."

No known problem with contractors not submitting applications !
What happens if no form stated in Scope ?

- ❖ New clause 50.4 says that if does not submit an application **BEFORE** this date, then gets lesser of either :
 - previous months amount due; or
 - the amount due this month.

Seems very harsh sanction for perhaps being a day late.
What happens if it isn't "in the form stated" ... which could be changed during the contract ? Seems very open to abuse.

Payment (2)

- ❖ New Final Assessment core clause 53.
- ❖ Not needed if Parties are operating the contract as written as compensation events implemented on a rolling basis.
- ❖ In reality, many projects don't achieve this AND new clause creates finality i.e. don't have an on-going potential liability.
- ❖ How does it work ?
 1. The *PM* makes final assessment after Defects Certificate issued.
 2. If *PM* does not do this, *Contractor* issues own assessment to the *Client* (no time limit).
 3. Either way, if the other agrees with it paid within 3 weeks.
 4. If don't, then can reach agreement and amount changed OR have to start the dispute process within 4 weeks.



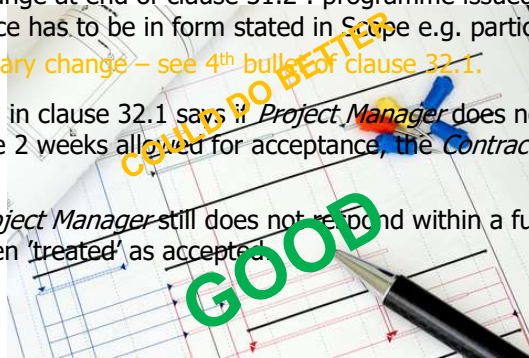
Payment (3)

- ❖ New 'progressive assessment' clause 50.9 in options C-F for Defined Costs.
- ❖ Idea is to stop a *Client* 're-evaluating' Defined Costs towards end of a contract to *Contractor's* detriment.
- ❖ How does it work ?
 1. The *Contractor* notifies *PM* that a 'part of Defined Cost' is ready for inspection.
 2. The *PM* has 13 weeks to inspect and response is acceptance, or notification that further records required or of errors.
 3. *Contractor* has 4 weeks from notification to rectify.
 4. The *PM* then has 4 weeks from ??? to accept or notifies correction.



The Accepted Programme

- ❖ Minor change at end of clause 31.2 : programme issued for acceptance has to be in form stated in Scope e.g. particular software.
Unnecessary change – see 4th bullet of clause 32.1.
- ❖ New para in clause 32.1 says if *Project Manager* does not respond within the 2 weeks allowed for acceptance, the *Contractor* may notify this.
- ❖ If the *Project Manager* still does not respond within a further **one** week, then 'treated' as accepted.



Early warning clauses

- ❖ Main changes :
 - Now clause 15
 - Early Warning Register (EWR) instead of confusing Risk Register. Indeed, no mention of 'risk' in EW clauses.
 - EWs = 'matters' that could increase T, £ & Q, so can be emerging risks or issues that are notified.
 - Regular early warning meetings at interval stated in Contract Data.
 - Encourages Subcontractor to attend an early warning meeting if it would assist in deciding actions.
 - At an early warning meeting, actions are reviewed for being done & effectiveness, before EWR updated.

Early warning clauses : contractual contradictions

Does the EWR record

- ❖ “the **way** in which the effects of the matter are to be avoided or reduced” (last sentence of 11.2(8))
- ❖ “the **actions**” decided upon at the early warning meeting (as per clause 15.3) or
- ❖ “the **decisions**” that the *Project Manager* records as a result of the early warning meeting (as per clause 15.4) ?

Early warning clauses: operational issues

- ❖ On the best run sites, “matters” are resolved at the lowest possible level ASAP^{Practically} by *PM* delegates. Having a regular early warning meeting encourages the actions to be monitored, but may also encourage decisions and actions to be delayed.
- ❖ Why can’t the *Supervisor* notify (still) ?
- ❖ If using a cloud-based NEC admin system, the system – not the *PM* – adds notified matters to the EWR.
- ❖ Isn’t the *Contractor* best placed to ‘own’ the EWR as :
 - has Subcontractors reporting to it and
 - contractually owns most of the risk / issues ?

Early warning clauses: operational issues

- ❖ What about positive '**opportunities**' ?
- ❖ On best projects, seeking out opportunities is a pre-occupation of the management ... they don't wait until there is a problem !!
- ❖ Very easy to modify wording in 15.1 to "changes" vs "increases" to Prices / "delays" to Completion / Key Dates and add "or improves" to performance in use.

Compensation events : Some changes

- ❖ In short forms, simplification of compensation event process to that in the NEC3 **Professional Services Short Contract**
- ❖ 2 new compensation events : for cost of non-accepted proposed instructions & contract specific CEs stated in the Contract Data.
- ❖ One *fee percentage* (which also affects payment under options C-F)

Compensation events : Timescales

Timescales, following reminder notifications, for the *Project Manager* to :

- ❖ respond to a notification of a CE
- ❖ respond to a *Contractor's* quotation
- ❖ make his or her own assessment, otherwise "treated as accepted" is still 2 weeks.

Why, when the *Project Manager* has 1 week, 2 weeks and 3 weeks to make original response ?

Why, when for the programme, it is 1 week ?

Compensation events : Clarification on the dividing date (1)

- ❖ First part of clause 63.5 states :

"A delay to the Completion Date is assessed as the length time that, due to the compensation event, planned Completion is later than planned Completion as shown on the Accepted Programme current at the dividing date."

- ❖ What is the 'dividing date' ? See clause 63.1

"For compensation events which arise from the *PM* or *S* giving an instruction or notification, issuing a certificate or changing a decision, the dividing date is the date of that communication.

For other compensation events, the dividing date is the date of the notification of the compensation event."

Compensation events : Clarification on the dividing date (2)

Change to clause 63.5 and 63.1 gives more clarity on the 'dividing date' by

- ❖ separating forecasts from actuals in an assessment,
- ❖ clarifying which Accepted Programme is used to assess the effect of a compensation event and
- ❖ ties assessment of time and cost closer together.

Compensation events: More precision on how time is calculated

63.5 "A delay to the Completion Date is assessed as the length of time that, due to a compensation event, planned Completion is later than planned Completion as shown in the Accepted Programme current at the dividing date."

"The assessment takes into account

- any delay caused by the compensation event already in the Accepted Programme and
- events which have happened between the date of the Accepted Programme and the dividing date."

Compensation events : Final Highlights

- ❖ New clause 65 gives more comprehensive direction on proposed instructions (and pushes back old 65 to 66).
- ❖ Change to 66.3 where "assessment of implemented compensation events is not revised except as stated in these *conditions of contract*" e.g. changed assumptions, changed decision, dispute procedure etc.

The two Schedules of Cost Component

There is a
(normal/full) Schedule of Cost Components (SoCC)
and a
Shorter Schedule of Cost Components (SSoCC)

Options A & B :

11.2 (23) Under options A and B, the change in Defined Costs for a compensation event is calculated using the SSoCC.

Options C to E :

11.2 (24) Under options C to E, Defined Costs, whether for :

- ❖ a compensation event to adjust the Prices or
- ❖ to reimburse the *Contractor their accrued costs*

is calculated using the full SoCC.

No reference is made from one Schedule to the other unlike in NEC3

Key (S)SoCC changes

- ❖ In Shorter SoCC, *Contractor* tenders People Rates, but even looser criteria apply for calculating those without a rate.
- ❖ Almost all percentages no longer exist & are paid for either:
 - at cost e.g. no % for WA O/Hs, no % for People O/Hs OR
 - included in rate e.g. no % for MorF, and no % for design.
- ❖ Subcontractors are now part of both SoCCs, rather than, in NEC3, being Defined Cost and not in SSoCC.
- ❖ One *fee percentage* for both direct & subcontract costs
- ❖ Under options A & B, get 'fee-on-fee' for subcontract costs incurred in accordance with the subcontracts when a compensation event occurs (as per NEC3&4, options C to E).
- ❖ There is a version of the (S)SoCC in the TSCs, PSCs & SC.

To summarise

A few **UGLIES**
A fair few **COULD DO BETTER** / **BADs**
But mainly **GOODs**

So Clients especially:
why aren't you using NEC4 ?
(and cutting down on unnecessary amendments)