

# INTRODUCTION TO NEC4

Peter Kerrigan  
LLB(Hons), FRICS, FCI Arb  
Barrister & Chartered Quantity Surveyor

Kevin McGuire  
BSc, LLB(Hons), DipAdj, FRICS, FCI Arb  
Solicitor & Chartered Quantity Surveyor

**KERRIGANS CONSTRUCTION LAWYERS**

[www.kerrigans.net](http://www.kerrigans.net)

# The Course

- Primary objectives:
  - ◆ Ensure that all participants are broadly familiar with the NEC4 suite and are aware of the main variances between NEC3 and NEC4.
- Content
  - ◆ Background to NEC and its development;
  - ◆ Terminology changes in NEC4;
  - ◆ Key changes to the core clauses;
  - ◆ Changes to the SCC/SSCC;
  - ◆ Key changes to secondary options;
  - ◆ Other notable changes; and
  - ◆ Questions.

# The NEC

- The NEC suite of contracts is published by the Institution of Civil Engineers (ICE).
- The NEC website says:

“NEC is a family of contracts that facilitates the implementation of sound project management principles and practices as well as defining legal relationships.”

# NEC Core Principles

- **Flexibility** - Idea is that parties construct contract from the core clauses, main options and secondary options avoiding the need for bespoke amendments.
- **Simplicity and clarity** - The contract is written in the present tense, in plain English and avoids the use of mandatory words.
- **Stimulus for good management** - The NEC focuses on real-time management. This can lead to high demands on management and administration time. As with any contract, both parties need to understand the process and ensure that it is properly resourced.

# Development of the NEC Suite

- NEC suite now in its fourth incarnation known as “NEC4”
- Published on 22 June 2017.
- Introduces four new contracts:
  - ◆ Professional Service Subcontract
  - ◆ Term Service Subcontract
  - ◆ Design Build Operate Contract
  - ◆ Alliance Contract

# NEC4 Key Objectives

- In drafting NEC4, NEC had three key objectives:
  - ◆ Provide greater stimulus to good management.
  - ◆ Support new approaches to procurement that improve contract management.
  - ◆ Inspire increased use of NEC in new markets and new sectors.

# NEC4 ECC - Main Options

- There are six Main Options:
  - ◆ A - **Priced** Contract with **Activity** Schedule
  - ◆ B - **Priced** Contract with **Bill** of Quantities
  - ◆ C - **Target** Contract with **Activity** Schedule
  - ◆ D - **Target** Contract with **Bill** of Quantities
  - ◆ E - **Cost reimbursable** Contract
  - ◆ F - **Management** Contract

# NEC4 Core Clauses

- The core clauses in the NEC4 suite of contracts are:
  - ◆ General
  - ◆ Contractor's main responsibilities
  - ◆ Time
  - ◆ Quality Management (was Testing and Defects)
  - ◆ Payment
  - ◆ Compensation Events
  - ◆ Title
  - ◆ Liabilities and insurance (was Risk and Insurance)
  - ◆ Termination



# Secondary Option Clauses

- The Standard Secondary Option clauses include:
  - ◆ Options W1 – W3: dispute resolution (W3 is new)
  - ◆ Options X1 – X22 (not all the secondary options can be used with all the main options).
  - ◆ Option Y(UK)1: project bank account.
  - ◆ Option Y(UK)2: The Housing Grants, Construction and Regeneration Act 1996 (Construction Act 1996) (dealing with payment and suspension).
  - ◆ Option Y(UK)3: The Contracts (Rights of Third Parties) Act 1999.
  - ◆ Option Z: additional conditions of contract.

# Terminology Changes

- *“Client”* replaces *“Employer”* across the suite, apart from the NEC4 Supply Contract (SC) and Supply Short Contract (SSC) where this role is performed by the *“Purchaser”*.
- All of the contracts use the term *“Scope”* for the document that sets out the work being provided.
- *“Early Warning Register”* replaces the *“Risk Register”* to avoid confusion with the generic project risk register.

# Clause 10.1: “Mutual trust and co-operation”

- NEC3, clause 10.1 has been re-formatted in NEC4 and now states:
  - “10.1 The Parties, the Project Manager and the Supervisor shall act as stated in this contract.
  - 10.2 The Parties, the Project Manager and the Supervisor act in a spirit of mutual trust and co-operation.”
- Clause 10.1 obliges the Parties, the Project Manager and the Supervisor to do everything that the contract states they do.
- Clause 10.1 is the only clause which uses the future tense and the only provision that uses the word “shall” - the effect of that is that “shall” does not have to be used elsewhere in the contract.

## Clause 10.2: “Mutual trust and co-operation”

- Clause 10.2 also requires the same people to act in a spirit of mutual trust and co-operation.
- That is particularly needed in managing parts of the contract such as early warning, payment, programme and compensation events.
- NEC4 user guide (vol.4) confirms that:

“...this clause does not change the obligations of the Parties, the Project Manager and the Supervisor as set out in the contract.”

# Clause 17.1: Ambiguities and inconsistencies

- Now under the heading “Requirements for instructions”.
- Wording of clause 17.1 is very similar but:
  - ◆ NEC3 – PM gives an ‘instruction’ resolving the ambiguity/inconsistency.
  - ◆ NEC4 – PM ‘states’ how the ambiguity/inconsistency should be resolved.
  - ◆ Is that significant?

# Clause 31.3: Programme

- Clause 31.3 now includes the following words:

“If the *Project Manager* does not notify acceptance or non-acceptance within the time allowed, the *Contractor* may notify the *Project Manager* of that failure. If the failure continues for a further one week after the *Contractor’s* notification, it is treated as acceptance by the *Project Manager* of the programme.”

- Clause 31.3 provides for deemed acceptance of the programme by the *Project Manager* if he/she fails to respond within the time allowed to a programme offered by the *Contractor* for acceptance.

# Clause 32.1: Programme

- Reference to compensation events in clause 32.1 is now deleted.
- Clause 31.2 requires each programme to show “the order and timing of the operations which the *Contractor* plans to do in order to Provide the Works”.
- Therefore, both “implemented” and “unimplemented” compensation events must be shown.

# Payment

- Two anomalies in NEC3 which often resulted in the addition of Z clauses:
  - ◆ the starting point for an interim payment under NEC3 was assessment by the *Project Manager*; and
  - ◆ no definitive final account process.
- Both have been addressed in NEC4.



# Clause 50.2: Payment

- NEC3, clause 50.4 (unamended), the *Project Manager* was required to make the assessment and consider any application by the *Contractor*.
- NEC4, clause 50.2 now requires the *Contractor* to make an application for payment before each assessment date.
- No application, no payment (NEC4, clause 50.4)

# Clause 53: Finality of Assessments

- Clause 53 provides that:
  - ◆ The *Project Manager* assesses and certifies the final amount due, if any, no later than 4 weeks after the Defects Certificate or 13 weeks after a termination certificate (clause 53.1).
  - ◆ The *Contractor* may issue its own assessment of the final amount due to the *Client* if the *Project Manager* fails to do so within the required time periods (clause 53.2).
- An assessment of the final amount due is conclusive evidence of the final amount due immediately (clause 53.3).
- Conclusivity is subject to what is essentially a 4 week time period unless either party invokes the disputes resolution procedures set out in clause 53.3. Clause 53.3 must be followed.

# Agreeing Defined Cost

- In addition to the 'final accounting' procedure, the cost based contracts (ECC Options C, D, E and F) now include provisions for Defined Cost and Disallowed Cost to be reviewed and accepted progressively (clause 50.9)
- Under these Options:
  - ◆ *Contractor* notifies the *Project Manager* when the Defined Cost for part of the works is finalised and ready for review.
  - ◆ *Project Manager* must review this within 13 weeks and either accept, or advise of any errors.
  - ◆ If the *Project Manager* fails to do this within the required timescale, the *Contractor's* Defined Costs are treated as though they have been accepted.

# Clause 60.1(20): Compensation Events

- Clause 60.1(20) introduces a new compensation event:

“The *Project Manager* notifies the *Contractor* that its quotation for a proposed instruction is not accepted.”
- *Contractor* is now entitled to recover the cost of preparing the quotation. Clause 11.2(23) in Options A and B has also been amended.

## Clause 60.1(21): Compensation Events

- Clause 60.1(21) provides for additional compensation events to be listed in part one of the Contract Data.
- Intended to allow the parties to agree additional compensation events where appropriate without the need for Z clause amendments.

# Clause 61.3: Compensation Events

- Clause 61.3 now requires the *Contractor* to notify a compensation event within 8 weeks “of becoming aware that the event has happened”.
- NEC Guidance notes confirm that the time limit starts:

“when the *Contractor* is aware that the underlying event occurs, **not** when the *Contractor* becomes **aware that it is a compensation event**”.

# Schedule of Cost Components and Fee

- Not all contracts in the suite have a Schedule of Cost Components (SCC).
- Where the contract includes a SCC, it is used to assess Defined Cost.
- Amendments have been made to simplify the SCC:
  - ◆ Subcontractor costs have been moved to the SCC and payment of these is now consistent across all Main Options.
  - ◆ There is now only one *fee percentage* applied to Defined Cost and no separate *fee percentage* for subcontracted works.

# Schedule of Cost Components and Fee

- Options A and B:
  - ◆ the **Short Schedule** of Cost Components (“SSCC”) is used in Main Options A and B;
  - ◆ **pre-priced approach** for people cost;
  - ◆ **percentage** for **people** overheads **removed**; and
  - ◆ **percentage** for **design** overheads **removed**.
- Options C, D and E:
  - ◆ the SSCC has been removed;
  - ◆ **percentage** for **Working Areas** overheads **removed**;
  - ◆ **percentage** for **design area** overheads **removed**; and
  - ◆ note change to item 11 in SCC (People) in recognition of flexible work patterns.



# Assessing Delay

- In order to assess delay caused by a compensation event, one has to ascertain the delay to planned Completion caused by the compensation event using the Accepted Programme - but which Accepted Programme do you use?
- This year, clause 63.5 was amended as follows:
  - “*The assessment [of any delay to the Completion Date arising from a compensation event] 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.*”
- The “dividing date” is defined in clause 63.1 as either the date of communication from *Project Manager/Supervisor* or notification of the compensation event by the *Contractor*.

# Assessing Delay

- To establish the delay caused by a compensation event, users should first recognise the impact of:
  - ◆ alterations to the Accepted Programme resulting from other compensation events occurring prior to the dividing date;
  - ◆ delays to planned Completion resulting from other causes of delay occurring prior to the dividing date and which are not compensation events; and
  - ◆ better or worse actual progress for activities that have started or should have started prior to the dividing date.
- Once this is done, the impact of the compensation event in question can be determined.

# Liabilities and Insurance

- Section 8 in the NEC3 contracts dealing with risks and insurance has been revised:
  - ◆ “Risks” has been changed to “liabilities” - avoids confusion with the term “risk” used elsewhere in the NEC4 contracts.
  - ◆ *The Contractor’s liabilities are now set out in detail in clause 81.*
  - ◆ Clause 84.2 now requires insurance policies to include a waiver of subrogation rights against the parties.

# Resolving and Avoiding Disputes

- This section is now entitled “Resolving and Avoiding Disputes” rather than “Dispute Resolution”.
- Options W1 and W2 remain but include a new “*escalation and negotiation*” step.
- Any dispute is first referred to senior representatives.
- Senior representatives essentially have a four week period within which to meet and try to reach a negotiated solution. This takes place prior to any formal proceedings being commenced.
- Process is mandatory under Option W1 (used if the HGCRA does not apply).
- Process is consensual where Option W2 applies (when HGCRA applies).

# Option W3: Dispute Avoidance Board

- New Option W3 in the ECC only.
- Can be used if HGCRA does not apply.
- Appoint a standing Dispute Avoidance Board (DAB) as an alternative to adjudication.
- DAB is appointed at the start of the project and makes regular visits to the project site.
- If a “potential dispute” does arise, it is referred to the DAB. Process is mandatory if Option W3 is selected.

# Option W3: Dispute Avoidance Board

- If the parties are not able to settle the potential dispute with the DAB's help, the DAB provides a non-binding recommendation for resolving it.
- The parties may accept the DAB's recommendation.
- If a party is dissatisfied with the recommendation, it must give notice of intention to refer the dispute to the tribunal within four weeks.
- If W3 is selected, a dispute cannot be referred to the tribunal (courts or arbitration) for final determination unless it has first been referred to the DAB.

# Option X4: Guarantees

- Option X4 has been renamed “Ultimate Holding Company Guarantee” rather than “Parent Company Guarantee”.
- The *Client* may:
  - ◆ require a guarantee from the *Contractor’s* ultimate parent; or
  - ◆ accept a guarantee from an intermediate holding company if it is satisfied with the financial strength of the intermediate company.

# Option X8: Undertakings

- Previously, only the NEC3 Professional Service Contract included a section on collateral warranty agreements.
- New secondary Option X8 is named “Undertakings to the Client or others”.
- It provides for the provision of collateral warranties from:
  - ◆ *Contractor* to third parties.
  - ◆ Subcontractors to the *Client* and third parties as required.



# Option X10: Information Modelling

- New terminology “Information Modelling”, rather than BIM.
- Reflects the fact that information modelling:
  - ◆ Is not restricted to buildings, but can be used for all forms of construction.
  - ◆ Is relevant world-wide and not applicable exclusively to the UK market.

# Option X11: Termination at Will

- Allows the *Client* to terminate at will.
- If the *Client* is to have a right to terminate at will, this must be specifically chosen as a secondary option.
- Applies across all NEC4 contracts.

# Option X15: Design Liability

- Option X15 has been substantially re-written.
- Intended specifically to support design and build (D&B) contracting.
- *The Contractor:*
  - ◆ Is required to effect and maintain professional indemnity insurance.
  - ◆ Provides certificates confirming that the insurance required is in force (before and after the *defects date*).
  - ◆ Must design the works using the skill and care normally used by professionals designing similar works (note changed wording).
- NEC4 reverses the burden of proof. *Client* now has to prove that the *Contractor* failed to exercise skill and care in its design.

# Option X16: Retention

- New clause X16.3 which provides that the *Contractor* may give the *Client* a retention bond.
- Requirement for a retention bond must be stated in the Contract Data or agreed by the *Client*.
- *Project Manager* has to accept the proposed bank or insurer.
- Form of bond will be as set out in the Scope.

# Other Changes

## Contractor's Proposals

- New core clause 16 introduces a value engineering process.
- Provides that the *Contractor* may propose a change to the Scope that will reduce the cost of the Works, which the *Project Manager* may accept and instruct, not accept or request a quotation prior to making a decision.
- In addition, a new secondary Option X21 (whole life cost) allows the *Contractor* to propose a change to the Scope in order to reduce the cost of operating and maintaining an asset.
- Under Options A and B, a value engineering percentage (identified in the Contract Data) is applied when assessing the compensation event (clause 63.12).
- Under Options C and D, the *Contractor* can potentially benefit under the pain/gain mechanism.

# Other Changes

## Bribery and Corruption

- A new core clause (clause 18) imposes express obligations on the *Contractor*, both directly and in relation to its supply chain, not to commit Corrupt Acts.
- The *Client* has an additional reason to terminate in certain circumstances if the *Contractor* commits a Corrupt Act (clause 91.8).

# Other Changes

## Assignment

- New core clause 28 obliges each party to notify the other if it intends to assign the benefit of the contract or any right under the contract.
- *Client* is not able to assign such benefits or rights if the assignee does not intend to act in a spirit of mutual trust and co-operation.

# Other Changes

## Confidentiality

- New core clause 29 deals with confidentiality and disclosure of project information.
- NEC3 PSC was the only contract in the NEC3 suite that previously provided for this.
- This type of provision was often included in the other NEC3 contracts by way of a Z clause amendment.





# Questions?