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1 Introduction

The construction industry has developed to be complex in nature which has in turn contributed to the adversarial culture that the industry is infamous for (Jaffar, Abdul Tharim, Shuib, 2011, p.193; Cheung *et al.* 2008, p.942).

The relationship between the parties involved in a construction project comprises a set of interrelated interests that require coordination of time, resources and communication (Harmon, 2003, p.121).

Conflicts are inevitable and, if not resolved, there will be consequences on both of the progress of the construction project and the relationships between the parties (Harmon, 2003, p.121).

This report is prepared to deliver a set of recommendations and advice to the Contractor who was awarded a project that comprises 80 housing units in Skye, Scotland under NEC3 ECC conditions of contract and has encountered some problems in the post contract stage of the project.

The dispute has arisen between the parties due to several incidents. These issues will be discussed and analysed in the context of sections of this report.

2 Assumptions

The following assumptions were considered in this report:

- Submitted to the 'Contractor'.
- NEC3 ECC Core Clauses.
- Main Option B (Priced contract with bill of quantities).
- W2 incorporates adjudication in the UK when the HGCR Act 1996 applies.
- X7 incorporates Delay damages.
- X16 incorporates Retention.
- Y(UK)2 incorporates HGCR Act 1996 as amended.

3 Law Governing Construction Contracts

In this section, the general principle of law governing construction contracts will be discussed to act as a guideline that will lead the investigation of the current status of the project that will be further illustrated in the next sections of this report.

For a contract to be valid, it has to be enforceable at law, imposing rights and obligations. The following elements of formation are essential for a contract to be valid *ab initio* i.e. valid from the beginning:

- Agreement;
- Intention;
- Consideration (not required in Scotland).

Express terms can be either written in the contract document or conveyed verbally.

Implied terms are not mentioned in the contract but were part of the intent of the parties and they may be imposed by relevant legislation. Under tort law, parties still have obligations to each other regardless of the contract as each party has a duty of care to the other.

There are extensive standard forms of contracts tailored for the construction industry to define relationships between parties. The contract documents define the work to be performed along with cost and time allocated for the project.

The sources of contract law are common law and statute law; they are of different origin but with same objectives.

“The Housing Grants, Construction and Regeneration Act”, also known as the “Construction Act”, has played an important role as part of the law governing the construction industry (Out-Law 2011).

Part 8 of the “Local Democracy, Economic Development and Construction Act” that came into force in relation to construction contracts entered into in or after 1 November 2011 in Scotland, has made several amendments to the “Construction Act” (Out-Law 2011). The amendments main intentions are (Out-Law 2011):

- “to increase clarity and certainty as to payment in construction contracts;
- to introduce a 'fairer' payment regime, and improve rights for contractors to suspend their work in non-payment circumstances; and
- to make adjudication more accessible for the resolution of disputes.”

4 Conditions Guiding Payment in the NEC3 ECC

One of the major aspects of dispute in this project is late payment. Late payment can lead to detrimental consequences to the project, as it will affect the Contractor's cash flow and accordingly, progress. As a matter of fact, late payment or non-payment are considered as material breach of the contract that give the right to the Contractor to suspend the works or even terminate the contract without prejudice to any other right.

A significant change has been introduced by the ECC in relation to terms of payment, which made the Project Manager responsible for the regular assessment of the amount due to the Contractor (Mitchell and Trebes, 2012, p.6). The Contractor may submit payment applications, but it is not an obligation (Mitchell and Trebes, 2012, p.6).

The Project Manager is the only one responsible for making deductions from the amount due. Deductions can be made on the occasions of not receiving the first programme (clause 50.3), Completion is late (clause X7.1) and as Retention (clause X16.1).

Conditions of contract outline the interim payments process as following and as illustrated in Figure 1:

- The Project Manager decides the date of the first assessment (clause 50.1)
- The Contractor submits the payment application on or before the assessment date (clause 50.4)
- The Project Manager assess the amount due which is the Price for Work Done to Date, plus other amount to be paid to the Contractor, less amounts to be

paid by or retained from the Contractor, less previous payments, plus VAT required by law (clause 50.2)

- The payment becomes due, seven days after the assessment date (clause Y2.2)
- The final date for payment is fourteen days after the payment due date (clause Y2.2)

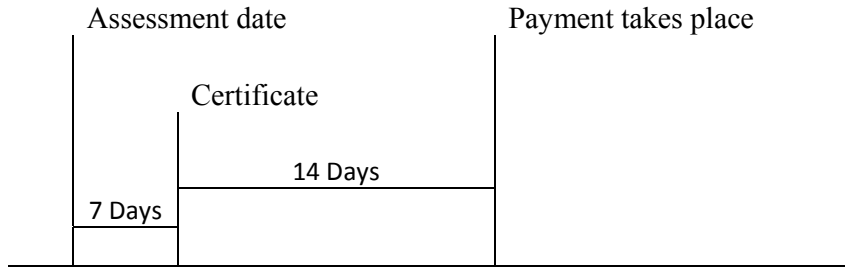


Figure 1: Times for payment – Y(UK)2

Payments cannot be withheld under this contract unless this intention is notified along with reason for withholding payment no later than seven days before the final date for payment (clause Y2.3).

According to clauses 51.2, 51.3 and 51.4, if a certified payment was made late or if the Project Manager did not issue the payment certificate as he should (in clause 51.1) or if the due amount was corrected in a later certificate because of Project Manager’s mistake, interest will be calculated and paid in the very next assessment.

Section 112 of the “Construction Act 1996” as amended by “Local Democracy Economic Development and Construction Act 2009”, states that “*the person to whom the sum is due has the right (without prejudice to any other right or remedy) to suspend performance any or all of his obligations under the contract to the party by whom payment ought to have been made (‘the party in default’)*”. However, this right cannot be exercised without giving proper notification which as stated in subsection

(2) of this Section to be at least seven days' notice before intending to suspend the works.

Furthermore, subsections (3A) and (4) of Section 112, held the 'party in default' liable to pay to the other party the cost and expenses incurred by that party as a result of suspending the works.

5 Conditions Governing Contractual Programme

The project has suffered delays due to several delaying events i.e. late payment, lack of workmen on site and late Project Manager's instructions. It is of high importance to manage the programme in an appropriate way in terms of the way it should be prepared and submitted, the way it should be maintained and how it can be used as a tool to assess changes and compensation events that will eventually, relieve the Contractor from paying Delay Damages to the Employer.

NEC3 ECC was introduced with an aim to reduce changes that occurs in construction projects (Mitchell and Trebes, 2012, p.20). Nonetheless, ECC contract acknowledges that changes in construction projects are inevitable and thus, it provides tools to handle impacts of such changes in a more efficient way (Mitchell and Trebes, 2012, p.20).

A programme is a very important tool in ECC contract, and it is not only important as a scheduling tool but also as a tool to control changes and compensation events (Mitchell and Trebes, 2012, p.20). ECC contract made that statement clear through imposing a hefty 25% deduction of all payments due if the Contractor does not provide the first programme to the Project Manager (clause 50.3).

There are several key terminologies in the ECC that are used to shape the programme, which are Contract Date (clause 11.2(4)), starting date, access date, Completion (clause 11.2(2)), Completion Date (clause 11.2(3)), planned Completion (clauses 31.2 and 63.3) and Key Date (clause 11.2(9)) (Mitchell and Trebes, 2012, p.20).

A programme that is properly loaded with resources and cost (clause 31) can be used as a project management tool that allows the Project Manager and The Contractor to monitor progress and to assess and control changes to the project and thus, it is very important that the Contractor should regularly revise the programme incorporating all the changes and compensation events which have happened or he expects to happen (clause 32) and also keep contemporary records of such events and accordingly, that can relieve the Contractor from paying delay damages to the Employer (Mitchell and Trebes, 2012, p.22, p.24; Gibson, 2008, p.77).

A revised programme should be submitted by the Contractor where a compensation event has happened or likely to happen along with a quotation that includes changes to the Prices and to the Completion Date (clause 62.2) (Mitchell and Trebes, 2012, p.35).

If the Completion Date is required to be maintained despite having compensation events, the Project Manager may ask the Contractor to submit alternative quotations based on different practicable methods he can adopt to deal with such compensation events to maintain the Completion Date, this can include optimizing the sequence of works or overtime or deploying additional resources or all together as may be required (Mitchell and Trebes, 2012, p.38).

6 Preparation and Submission of Contractual Claim

One of the most important features of ECC contract is the early warning of events that are likely to have an impact on progress and thus, cause delay. The contract requires either party to notify the other as soon as they are aware of any event that could delay completion (Gibson, 2008, p.77).

There are several events that have occurred which give rise to the need to submit claims by the Contractor i.e. typically an act of prevention by the Employer or the Project Manager (Hewitt, 2011, p.4).

Prior starting the preparation and submission of claims, certain matters need to be considered i.e. severity of the impact of event, value of the claim and relationships with the Employer (Hewitt, 2011, p.4, p.5).

Cash flow is critical to every contractor. If payments are not made or made in untimely manner, Contractor's profits, capital, financing and obligations under the contract are all impacted (Cushman *et al.* 2001, p.8). The Contractor has limited options in dealing with this type of claims (Cushman *et al.* 2001, p.9). However, the "Construction Act" gives the right to the Contractor to suspend the works without prejudice to any other right e.g. interest awarded on balances due. Nonetheless, the "Construction Act" requires certain procedures before exercising such right and hence, it is critical that notices required under the "Construction Act" should be sent in due course to the Employer i.e. at least seven days' notice before pulling workmen off site and suspending the works otherwise, the Employer may terminate the contract pursuant to clause 91.2.

NEC3 ECC contract contains provisions that allow the Project Manager to make changes to the works' information. However, ECC contract recognizes that as compensation events that may lead to an extension for the Completion Date and/or delay costs. However, ECC contract has very strict procedures that should be exercised to submit a claim for a compensation event.

Late instructions by the Project Manager falls under clause 60.1(1) of the compensation events clauses, if the Project Manager did not notify the Contractor about the relevant events pursuant to clause 61.1, the Contractor shall notify the Project Manager of such events pursuant to clause 61.3 within eight weeks of becoming aware of the event, otherwise the Contractor will not be entitled to a change in the Prices or the Completion Date.

Each compensation event claim shall be submitted along with a quotation comprising proposed changes to the prices and any delay to the Completion Date and accordingly (clause 62.2), the quotations will be assessed by the Project Manager, and if the Project Manager does not reply within the time allowed, the Contractor has to notify the Project Manager to this effect and again if the Project Manager does not reply to the notification within two weeks, that shall constitute as an acceptance of the quotation by the Project Manager (clause 62.6).

Contractor's culpable delays should be dealt with extreme caution, as they will be considered as concurrent delays that will decrease or even eliminate his entitlement for prolongation costs and on the worst scenario these delays might compound to be more than his entitlement for extension of time and accordingly, he will be liable to pay delay damages for the Employer (clause X7).

After going through the principles guiding claims, it is worth mentioning that for a claim to be successful, it should include four essential elements i.e. cause, effect, entitlement and substantiation (Hewitt, 2011, p.49).

7 Dispute Resolution Methods

It is evident that the relationships between the project's parties have deteriorated after the 10th month of the project. The dispute has emerged after the project has been delayed due to late payment, lack of workmen on site and late Project Manager's instructions.

Dispute resolution methods are mainly categorized under two main categories i.e. "non-adversarial" and "adversarial" methods. "Non-adversarial" methods tend to be quicker, cheaper, least harmful to relationships and more private when compared to "adversarial" methods.

The current situation of the project, where payments have not been made and workmen have been pulled off site, dictates that the simplest method of dispute resolution i.e. "Negotiation" is not effective at this point and thus, it can be time consuming. However, it is recommended that the least adversarial method should be adopted first.

"Mediation" is a good starting point that can help in resolving the dispute. This method is informal process that involves one or more independent parties that can help the project's parties reach a settlement (Hackett, Robinson and Statham, 2007, p.329). However, the mediator acts only as an advisor that has no authority to impose decisions (Hackett, Robinson and Statham, 2007, p.329). "Conciliation" is similar to "Mediation" but the conciliator can come up with proposed solutions.

Similarly, “Neutral evaluation” method is private and non-binding, but it usually involves a legally qualified third party that can help evaluate the situation and advice on the probable outcome at trial which will be the base of settlement discussions.

“Expert determination” method is considered as a transition between the least adversarial and more adversarial methods. This method involves the participation of an independent expert who gives binding decisions. This method is not famous within the construction industry.

“Adjudication” method is known to be the solution to the issues of the related high cost and lengthy process associated with arbitration and litigation. “Construction Act” made it mandatory on all construction contracts to include such provision and if a contract contains provisions that are not compliant with the Act, the Act would impose statutory adjudication that allows any party to refer to adjudication (Hackett, Robinson and Statham, 2007, p.329). After referring the dispute to adjudication, a binding and enforceable decision will be made within 28 days irrespective of the complexity of the dispute (Hackett, Robinson and Statham, 2007, p.329).

“Arbitration” and “Litigation” methods are considered as the most adversarial methods, and it is recommended that these methods should not be exercised until the above methods are exhausted, and that they should be left as a last resort as they are expensive, time consuming and are destroying relationships.

8 NEC3 ECC vs. FIDIC Red Book

In this section, the discussions made in the previous sections through NEC3 ECC form of contract will be presented in the context of FIDIC 1999 (Red Book).

The two forms of contract will be compared in regards to the following main criteria:

Programme

Unlike NEC3 ECC where the programme is considered as a contract document, FIDIC does not recognize the programme as a contract document despite the fact that the Contractor is required to provide the Employer with the programme within 28 days from the Commencement Date (clause 8.3).

In FIDIC, there are no penalties imposed if the programme is not submitted. On the other hand, ECC contract imposes a hefty deduction of 25% on all payments due if the first programme is not submitted.

In both forms of contract, the Contractor should regularly update the programme incorporating all the changes, which will eventually serve as an important tool to assess and control changes.

In NEC3 ECC, progress is assessed against the contract programme. In FIDIC, while the programme is not a contract document, the Contractor is still obliged to perform with due expedition and without delay (clause 8.1).

Variations / extension of time / claims

FIDIC is considered to have a traditional approach in terms of variations, extension of time and claims (Heaphy, 2011, p.7) in comparison to NEC3 ECC, which has introduced the early warning system that enables either party to notify the other when they become aware of any event that could negatively affect any aspect of the project (Hide, 2010, p.111).

Under ECC contract, all these issues are included in the compensation events section (clause 60). On the other hand, FIDIC has provisions for evaluation of variations (clause 13), specific clauses for extension of time (clause 8.4) and a separate section for claims (clause 20.1) (Heaphy, 2011, p.7).

As discussed previously, in case of non-payment, the Contractor has the right to suspend work after satisfying the notification procedure under the ECC contract and the “Construction Act”. Similarly, FIDIC gives the right to the Contractor to suspend work under clause 16.1 after giving a notice of not less than 21 days to the Employer. The FIDIC is giving the Contractor an additional option in that regard to reduce the rate of work.

Late instructions and variations claims can be dealt with in FIDC by giving notice to the Engineer not later than 28 days after becoming aware of the event under clause 20.1 and pursuant to clause 8.4 which entitles the Contractor for an extension of time for completion and any additional payment if he suffers any delay or prevention caused by Employer or Engineer.

Dispute Resolution

Both the ECC and FIDIC have introduced an independent dispute resolution method as part of the contract, ECC contract has adjudication while FIDIC has dispute adjudication board (DAB) (Heaphy, 2011, p.8). They are essentially the same in principle and have been introduced to overcome the relatively higher cost and longer process of arbitration and litigation.

DAB comprises three members, one nominated by the Employer, one nominated by the Contractor and the third one is nominated by both Employer and the Contractor. DAB provides a better time frame to reach a decision i.e. 84 days when compared to the 28 days in adjudication which is considered as a limitation due to time pressure that can force the adjudicator to make mistakes.

The difference between DAB and adjudication in terms of reaching a decision is that if a party refuses to abide by the DAB decision, the other party will not be able to get immediate enforcement, while in adjudication as supported by the “Construction Act”, decisions are temporarily binding unless and until it is changed by arbitration or litigation (Glover, Hughes and Thomas, 2006, p.10).

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