NEC3 Compensation Events : agreeing contractual change promptly, amicable and constructively

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Objectives.

To give you some practical tips within a process for agreeing compensation events,
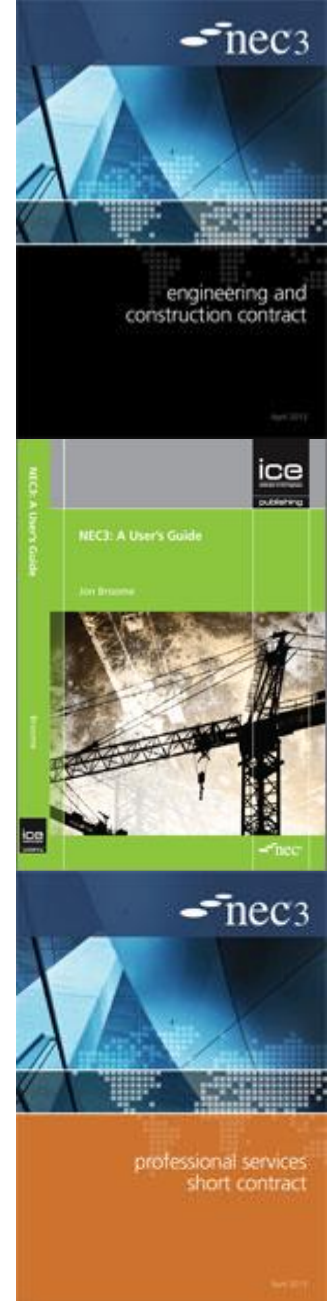so that :

- o they are agreed more quickly, amicably and accurately for less 'hassle'

- o the *Employer* gets better /more work for less

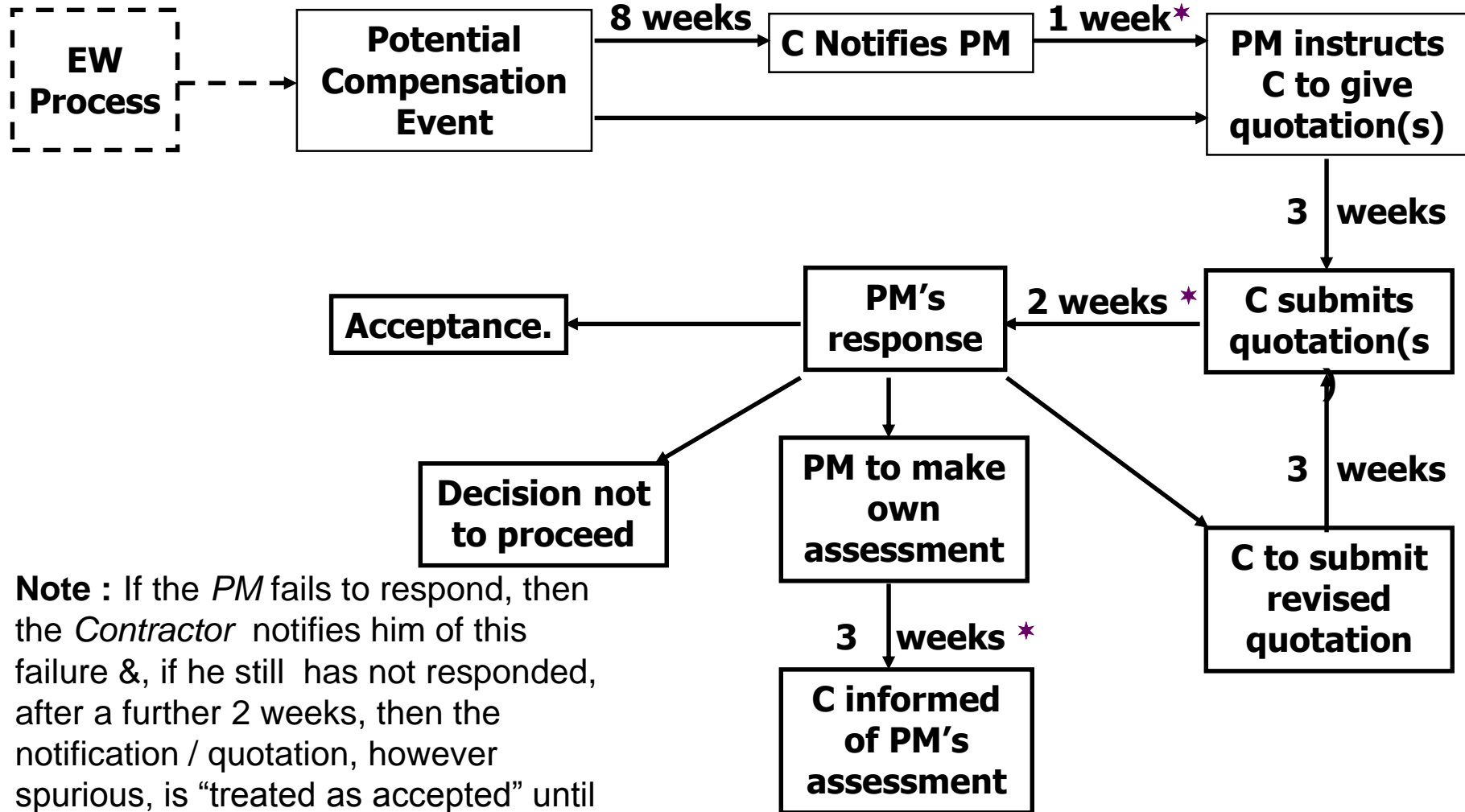- o the *Contractor* gets more profit.

Programme

1. A very little bit about me.

2. Overview of the compensation event process as defined in the contract

3. Process & Tips

4. Reflection & Take-Out

A very little bit about me & the NEC3.

❖ Genuine NEC Geek.

❖ Involvement in NEC goes back 20+ years when did a PhD on its practical use

❖ Contributions acknowledged in the full Engineering & Construction Contract.

❖ Authored 'NEC3 : A User's Guide'

❖ Led development of Professional Services Short Contract.

❖ Co-authored **b**i's on-line NEC3 Academy

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Compensation event process & timescales

EW Process → Potential Compensation Event

Potential Compensation Event — **8 weeks** → C Notifies PM — **1 week** ✱ → PM instructs C to give quotation(s)

PM instructs C to give quotation(s) — **3 weeks** → C submits quotation(s)

C submits quotation(s) — **2 weeks** ✱ → PM's response

PM's response → Acceptance.

PM's response → Decision not to proceed

PM's response → PM to make own assessment

PM's response → C to submit revised quotation

C to submit revised quotation — **3 weeks** → C submits quotation(s)

PM to make own assessment — **3 weeks** ✱ → C informed of PM's assessment

✱ **Note :** If the *PM* fails to respond, then the *Contractor* notifies him of this failure &, if he still has not responded, after a further 2 weeks, then the notification / quotation, however spurious, is "treated as accepted" until over-turned by Adjudication.

Why Pre-assess &/or agree rapidly ?

For the *Employer* :

❖ You know what you will pay

❖ For the *Contractor* to pre-price accurately, he has to have good quality information on which to base the quotation. He can then programme and work efficiently saving the *Employer* money.

❖ Rolling final account leading to agreed final account on or near to Completion

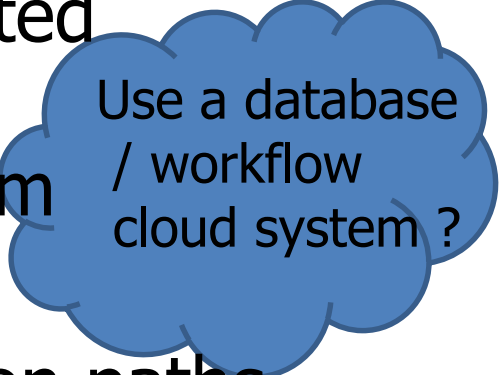❖ Less man hours, effort & acrimony vs. agreeing 'claim' at end

Why pre-assess &/or agree rapidly ?

For the *Contractor* :

❖ You know what you will receive

❖ As soon as agreed & you have done the work, you get paid under options A & B

❖ Ability & incentive to work efficiently & make extra profit through beating the adjustment

❖ Rolling final account leading to agreed final account on or near to Completion

❖ Less man hours, effort & acrimony vs. agreeing a 'claim' at end of contract.

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Pre-requisites: effective communications

❖ Discuss and agree orally, confirm and summarise "in a form which can be read copied and recorded"

❖ Create the right physical environment

❖ Have regular 'wrap up' meetings

❖ Develop pro-formas, inc. pre-formatted Excel worksheets for quotations

❖ Put in place a logging in & out system

❖ Extend system up, down & across

❖ Agree delegations and communication paths

❖ Have above set up before work starts

Use a database / workflow cloud system ?

Overview of process

Agree in approximate order :

❖ the cause & consequences (if not managed) of the CE

❖ the outcome that you want + any constraints

❖ the likely risks & how they will be allocated & any (other) assumptions

❖ the change in methods and resources including allowance for disruption

❖ any time delay

❖ the change in Defined Costs + Fee of the above four bullets

❖ communicate & iterate on the above

The Cause & 'Do-nothing' Consequences

❖ In order to identify Areas for Improvement
  o Identify under which CE heading it falls in order to allocate the cost to it
  o Separate out into changes / breaches by *Employer*, designer, *Project Manager*, *Supervisor* & other stakeholders to make parties accountable

❖ Agree the 'do-nothing' consequences of it as gives insight into how to solve it. E.g. if it is on the critical path and is happening now, then

  (a) solve now, not at next fortnightly meeting and

  (b) spend a bit more on direct costs to save delay & disruption costs.

The Outcome + Constraints

❖ Not the problem, but what you want instead e.g. no time delay or minimum cost, max certainty, a good physical description of the change etc. .

❖ Described clearly so that the *Contractor* can give an accurate quotation without lots of unnecessary risk in it. If not done, then likely to lead to a re-quote which is extra work for both parties.

❖ State any additional constraints upfront.

Assessing & managing risk - relevant clauses

63.6 : "Assessment of the effect of a compensation event includes risk allowances for cost and time for matters which have a significant chance of occurring and are at the *Contractor's* risk under this contract."

61.6 : "If the *Project Manager* decides that the effects of a compensation event are too uncertain to be forecast reasonably, he states assumptions about the event in his instruction to the *Contractor* to submit quotations. Assessment of the event is based upon these assumptions. If any of them is later to have been found to have been wrong, the *Project Manager* notifies a correction" and this is a CE under clause 60.1 (17).

Risks Management Theory

Risk Management has the following stages :

❖ Scope of study

❖ Identification

❖ Assessment

❖ Response Planning

❖ Response Implementation

Risks Management on CE's in Practice

1. Try to have a standard percentage no matter what the circumstances. Result : No agreement ever reached

2. Try to have a percentage based on the nature of work. Result : Percentage rarely agreed, with work usually pre-priced, done and assessed using records. Not sustained.

Risks Management on CE's in Practice

3. More sophisticated :

   ❖ Jointly identify and assess potential risks

   ❖ Think about what can be done to avoid or reduce likelihood of happening, then allocate outside (to the *Employer*) or inside the Prices (to the *Contractor*). If inside then to be priced in normal way.

   ❖ Minimise impact of occurrence and allocate outside or inside the Prices. If inside, then :

      o Potential premium = impact x likelihood

      o *PM* decides if good value for *Employer*.

4. Over complication to N'th level of detail at both parties expense.

Assumptions

❖ *PM* refines risks by stating as assumptions

❖ Failure to identify risk or being too broad =
    a high premium =
        failure to agree =
            refined assumption =
              re-work of quotation

❖ Too prescriptive = re-quotation under 60.1 (17) when assumption found to be wrong

❖ If *Contractor* identifies other risks & / or starts making assumptions when preparing quotation, then refer back to *PM* for clarification.

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Other ways of dealing with uncertainty

❖ Break the compensation event down into separate compensation events e.g. re-design and the price the re-design. This can include leaving out large unknown 'Plant' costs.

❖ Extend time scales by agreement under clause 62.5.

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Change in methods & resources

❖ *PM* can have input as is paying

❖ Use *Contractor's* expertise

❖ *PM's* who paid for *Contractor's* expertise thought that got good value.

Note : the literal meaning of 'preparing the quotation' is writing it up, not planning & organising the work.

❖ Once change in method is agreed then can agree change in resources

Assessing Delay & Disruption

❖ Use a standard assumption. Something like : "Provide a quotation for the direct costs only with the assumption of <u>no</u> delay and disruption. Any delay & disruption will be assessed at the end of the month as an additional compensation event together with other compensation events in which this same assumption is stated".

❖ Then 'wrap-up' delay & disruption as a CE under clause 60.1 (17) at the end of each & every month.

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Assessing disruption

❖ No magic formula, but
  - more detailed programme makes its assessment easier
  - programme is updated regularly
  - difference is a few days / a week at most each month vs weeks and months at end of contract
  - people who are there can agree it, versus year(s) old incomplete records

❖ Before re-submitting programme, agree a 'round up' CE for delay & disruption over past month

Delay Cost

❖ Related to extra time on site, but …

❖ Some of these cost are covered in percentages for People / Working Area overheads

❖ Do not pay twice if *Employer*

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Change in Defined Costs

❖ Put costs to change risk items, direct resources, disruption and delay

❖ Use Contract Cost Manual agreed at start of contract and added to once a resource has been used

❖ If the compensation events are worked out in the *Contractor*'s QS's room then supplier & Subcontractor rates, quotes, invoices & receipts etc. can be viewed there and then without need for photocopying / scanning.

❖ If a cost-based contract, can also be verified by *Project Manager*'s QS having read-only access to *Contractor*'s accounting system.

Communicate & Iterate

❖ Money is emotive. If *PM* does not understand where the time & costs are coming from then will automatically reject.

❖ Work out jointly before formal submission for acceptance

❖ Both parties gain advantages, as well as reducing 'negatives' acting on project

Overview Re-visited

Agree in approximate order :

❖ the cause & consequences (if not managed) of the CE

❖ the outcome that you want + any constraints

❖ the likely risks & how they will be allocated & any (other) assumptions

❖ the change in methods and resources including allowance for disruption

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Final **Review**

As an individual :

❖ What one 'take-out' from my talk can you take away and apply.

❖ Other practical tips ?

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- ❖ For our Q&A database, visit our Reachback desktop at http://reachback.builtintelligence.com or download as app from Google or Apple store.

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