CONSTRUCT

NEC ECC CONTRACT

EDT. 4
COMPENSATION EVENTS

MDA
Construction & Technology Attorneys

The 2025 MDA Attorneys Construct Journal is focused on the NEC3 and NEC4 engineering and construction contracts (NEC ECC).

In this fourth edition, MDA Attorneys discusses certain key aspects of the compensation events regime under both the NEC3 and the NEC4, providing key insights into its observations made during adjudications and arbitrations, including:

- Application of the time bar found in clause 61.3
- Criticism of the over-use of templates in the compensation event process
- Treated as accepted quotations
- Project Manager's assumptions vs Contractor's forecasts
- Defined cost
- Risks to the Employer created by the Project Manager's failure to accept programmes
- The inclusion of time risk allowances, particularly weather and ground conditions

The compensation event process is the cornerstone of the change management procedures in the NEC ECC. Core clause 6 is the longest clause in the contract reflecting its importance. The compensation events are listed in clause 60.1 with additional compensation events being found under certain payment options and secondary options.

Notification of compensation events

The NEC ECC differs from other standard form contracts in that certain compensation events are to be notified by the Project Manager, and others by the Contractor.

A time bar of eight weeks is applicable to the events which are to be notified by the Contractor. Events which are to be notified by the Project Manager are not caught by the time bar.

An interesting amendment in the NEC4 is the exclusion of an event requiring the Project Manager to notify a compensation event being a correction to an assumption made by the Project Manager (Clause 60.1(17)). The possible reading of this is that this compensation event becomes one that needs to be notified by the Contractor, and if not, one which is caught by the time bar. An interesting scenario then emerges where the Project Manager makes an ambitious assumption which is overstated and is later corrected. Here, if the compensation event has been assessed, the Contractor has most likely been compensated beyond the actual impact of the event. The correction is directed to reduce the compensation. However, if the Contractor does not notify the correction as a compensation event, the original assessment remains. This possible reading is the result of the streamlining of the wording in clause 61.3, but is an unlikely outcome given the additional reference to notifications by the Project Manager – i.e the notification of a correction to an assumption is an event notified by the Project Manager.

In the instance where a Project Manager's correction to an assumption is directed to reduce the compensation, the corrected compensation event is implemented, the previous amount assessed in respect of the compensation event is corrected in the following payment certificate, and interest on the correcting amount is paid (see clause 51.3). This provision acts as a safety net to the Project Manager when utilizing assumptions in respect of compensation events. Even so, it is very rare in practice to find a Project Manager making assumptions and this reluctance has a negative impact on the effectiveness of the change management procedures in the ECC.

Over-reliance on templates

It's common place to see inhouse templates being used for the notification of early warnings, Project Manager's instructions and compensation events. The intention is to ease the administrative burden and to provide a uniform set of documents for dealing with these key actions under the ECC.

In our experience an over-reliance of these templates is problematic. These are some of the problems:

- These templates are used across all contracts without any consideration for the payment option, Z clauses and/or Works Information/Scope.
- The Project Manager and Contractor disregard the provisions of the ECC and sometimes these communications are inherently contradictory. For example, a Project Manager, in responding to a compensation event quotation selects that the response is issued on the basis that a proposed instruction will not be given (clause 61.2) but then goes on to reject the quotation on different grounds.
- The use of these templates often accommodates laziness in setting out full details of the facts giving rise to the compensation event. When these templates come before a third party, they lack facts and context and need to be explained further.
- When instructions and notices fail to provide all of the necessary facts and required details, they are either not responded to, or they are rejected. This adds an additional burden to a contract which already has a reputation for being administratively intense.

Treated as accepted quotations

The NEC3 introduced the treated as accepted provisions following the widely held view that the compensation event procedure in the new engineering contract second edition was not working effectively because project managers were not cooperating. This approach has been carried through to the NEC4.

Where the Project Manager is recalcitrant, the situation arises where several reminder notices are issued culminating in a quotation becoming treated as accepted. However, is it possible to undo a treated as accepted quotation, particularly where the Contractor has not complied with the ECC in the preceding steps?

We have seen a defence to treated as accepted quotations whereby it is argued that, given the effect of essentially what is a deeming provision, that strict compliance with the notification and quotation provisions is required to ensure that the Contractor can enjoy the benefits.

Often notifications and/or quotations do not comply strictly with the requirements of the contract. Some examples include:

- The notice of compensation event is not issued within the eight-week period and is caught by the time bar in clause 61.3. A time barred notice cannot result in a treated as accepted compensation event.
- A Contractor will insert rates into a quotation which rates do not form part of the contract data and there has been no agreement with the Project Manager to use rates. This contravenes the requirements of defined cost.
- A Contractor uses a programme other than the accepted programme in its quotation.
- The Contractor submits the notice of compensation event and quotation simultaneously. This goes against the staged procedure contained in the ECC and opens the door for an Employer to argue non-compliance with the Contract.

In these circumstances the Contractor runs the risk that the treated as accepted quotation could be overturned in adjudication and/or by the tribunal.

Under clause W1 in the NEC3, where the Employer wishes to dispute a treated as accepted quotation, it must notify a dispute within four weeks or face the risk of being time barred. Under the NEC4, such a dispute would first be referred to the senior representatives and only thereafter does the strict notification period apply.

Assume or forecast? That is the question

Although the ECC is founded on the principle of cooperation, when it comes to compensation events, Project Managers often avoid their key obligations in working together with the Contractor to resolve the compensation event as intended.

This is particularly so when it comes to the issue of Project Manager's assumptions. Unlike other standard form contracts, where the works are confronted with an ongoing delay event, unless the Project Manager instructs an assumption, the Contractor is required to make a forecast. It should be pointed out that the Project Manager is obliged to make an assumption in such circumstances – however, such obligation is rarely complied with. In such a scenario, it is most likely that the party with the least insight into the extent of the delay event is the Contractor. The most obvious example here is the delay in granting access to the site or an instruction to stop the works. If the Contractor chooses to forecast the extent of this delay event, such forecast is nothing more than a guess. The other option to a Contractor is to refer the Project Manager's failure to make an assumption to dispute resolution.

The intention of the drafters of the ECC is that in such situations, the Project Manager issues an assumption which can be retrospectively adjusted to take account of the actual extent of the delay event. This allows for the accepted programme to be adjusted based on the actual duration of the delay event, ensuring accuracy in assessment.

Where the Project Manager does not instruct assumptions, the assessment is based on the Contractor's best guess forecast, which is usually inaccurate resulting in either prejudice to the Contractor or the Employer.

Defined Cost

The payment option selected and the details in the contract data prescribe the framework for determining defined cost. Often these details are misunderstood or overlooked, particularly in South Africa where the local standard form contracts provide for an adjustment to time related P&G where an extension of time is granted.

The compensation events mechanism entitles the Contractor to claim all defined cost associated with the compensation event. These include standing time/disruption cost, re-rating and additional material cost.

Although not necessary, a practice which is adopted by some Contractors and Project Managers is to agree to a schedule of defined cost upfront. This facilitates the administration of compensation events during contract execution.

Failure to accept programmes by the Project Manager

The ECC provides for the regular submission of revised programmes, together with the acceptance thereof by the Project Manager. There is only ever one accepted programme, being the most recent programme accepted by the Project Manager.

A common issue is the failure by the Project Manager to accept programmes on a regular basis. To be clear, this is not always the Project Manager's fault and can be attributed to the Contractor not submitting revised programmes or submitting non-compliant programmes.

The intention behind having a regularly updated programme is to ensure accuracy in the assessment of compensation events. Where this intention is met by the Contractor and Project Manager, the assessment of compensation events is done on the basis of a time impact analysis. However, where the programme is not regularly accepted, the assessment of compensation events becomes inaccurate and is done on the basis of an impacted as planned analysis, typically to the detriment of the Employer.

Time risk allowances

The assessment of compensation events should include for time risk allowances. Often such time risk allowances are not taken into consideration. The most obvious examples are weather delays and ground conditions.

Where a compensation event results in an extension to the completion date, the anticipated future weather delays (i.e. those which fall within the 10-year return) should be included in the extended period, regardless of the compensation event giving rise to the delay. Further, the defined cost for these weather delays should also be included in the Contractor's quotation.

In our next edition, MDA Attorneys will explore the topics of completion, defects, and termination under the NEC ECC. This will cover important concepts such as ‘key dates,’ the Employer’s rights when key dates are not achieved, and the treatment of latent defects.