

# Relational Contracts - NEC in Perspective

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*"The challenge to the construction industry and its advisers is not so much the NEC's suitability as a contract ... but rather how effectively existing practices can mould to the change of attitude and openness to new approaches that the NEC demands"* Philip Capper<sup>2</sup>

## Brief History of NEC

In 1985 The Institution of Civil Engineers (ICE) Legal Affairs Committee led a 'fundamental review of alternative contract strategies for ... design and construction with the objective of identifying the needs for good practice'. From the review came a strong recommendation that it was time to look afresh at conditions of contract.

The main reasons for this were:

- A proliferation of standard forms available
- The majority of projects are multi-disciplinary yet most contract forms are of a single disciplinary concept
- There was a high incidence of disputes and wastage of resources involved resolving them
- The origins of most forms of contract came before modern principles of project management were known
- A perception that clients wanted greater certainty of achieving project objectives.

The following year the ICE commissioned new style of contract to be developed, which was to meet the three key objectives of:

- Clarity and simplicity
- Flexibility of use
- Stimulus to good management.

A consultative version published 1991, which was trialled by the likes of BAA, Yorkshire Water, The Royal Hong Kong Jockey Club and ESKOM (South Africa).

## Philosophy and Ethos of ECC

The current published NEC contracts are:

- NEC Engineering and Construction Contract (ECC), 2<sup>nd</sup> Edition 1998
- NEC Engineering and Construction Short Contract (ECSC), 1<sup>st</sup> Edition 1999
- NEC Engineering and Construction Subcontract (ECS), 2<sup>nd</sup> Edition 1995
- NEC Engineering and Construction Short Subcontract (ECSS), 1<sup>st</sup> Edition 2001
- NEC Professional Services Contract (PSC), 2<sup>nd</sup> Edition 1998
- NEC Adjudicator's Contract, 2<sup>nd</sup> Edition 1998
- NEC Partnering Option X12

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<sup>2</sup> quoted in Dr Arthur McInnes The New Engineering Contract: A Legal Commentary'

There are also published Guidance Notes and Flowcharts to support the above documents.

These are currently all being revised as part of 'NEC3' and are due to be launched in June 2005 together with the following new publications:

- NEC Term Service Contract
- NEC Framework Contract
- NEC Procurement and Contract Strategies

The most popular form of NEC contract used is the NEC Engineering and Construction Contract (ECC), which is the contract between an Employer and a Contractor. The ECC has been developed to meet the current and future needs for a form of contract to be used in all types of construction, which improves upon existing standard contracts in a number of ways.

In terms of clarity and simplicity, the ECC is intended:

- To be written in ordinary language
- To contain minimal legalistic phrases
- To minimise subjective phrases such as 'fair', 'reasonable' and 'opinion'
- To have a user friendly structure
- For the actions of parties to be defined precisely so fewer disputes about who does what, when and how
- To have the procedural logic backed up by flow charts
- To have reasons for decisions stated.

For flexibility, the ECC is intended:

- To be a multi-disciplinary contract, for use in engineering or construction work
- That responsibility for design can be set with either party, in any proportion
- To give a choice of pricing mechanisms including lump sum, admeasure, target cost, cost reimbursable, management contract and construction management
- To give the choice of bolt on secondary options that allow the Employer to build up the contract to suit his policies
- To have international application.

In terms of being a stimulus to good management, this is probably the most important characteristic of the ECC. Every procedure is designed to contribute to rather than detract from the effectiveness for all parties.

The two principles the ECC uses to stimulate good management are:

- foresight applied collaboratively mitigates problems and shrinks risk, and
- clear division of function and responsibility helps accountability and motivates people to play their part.

In total, the ECC is intended to provide an up to date method for employers, designers, contractors and project managers to work collaboratively and to achieve their own objectives for their work more consistently than other forms of contract. This should lead to a much reduced risk of cost and time overruns and of poor performance of the completed projects which should give a much increased likelihood of achieving a profit for the contractor, subcontractor and suppliers.

## Drafting Philosophy

*“The ICE conditions of contract proceed on the basis that each side looks to its own interest. The NEC seeks to focus the interest of both parties on the project.”* Professor John Uff<sup>3</sup>

The change in drafting philosophy within NEC compares to other forms of contract in that most other major forms of contract seem to expand with successive editions with the result that many conditions of contract are filled with many terms that are rarely read and used.

The NEC describes a generic process for the management of problems that inevitably arise during a construction or engineering project. It attempts to tread a fine line between sufficient tightness, so that the contract participants follow the procedures, and sufficient looseness so that it can be interpreted in a way appropriate to the situation encountered.

Some of the main criticisms at the time of NEC being issued was that the drafting was not subjected to judicial interpretation. A response might be to ask whether in fact any precedence will indeed guarantee certainty of meaning? Further, it has been commented that the use of plain English could cause difficulties in certainty and proper legal construction. The intention is to draft contracts to give parties the best chance of achieving the projects' and their objectives, as surely it is desired that the parties and not the Courts administer contracts.

## NEC Contractual Arrangements

*“At the heart of the NEC is a new creed that Project Management techniques can be successfully written into a main contract to produce more co-operation, more efficiency and fewer disputes”* Professor John Uff<sup>4</sup>

In terms of project organisation, the NEC can be used in a variety of contractual arrangements. An Employer can appoint consultants to carry out design, quality checks, cost consultancy, archaeological work etc on individual or multiple projects using the NEC PSC. A consultant can use the PSC in turn as a sub-consultancy contract. An Employer for individual projects using the NEC ECC or NEC ECSC can engage a Contractor. In turn a Contractor can appoint sub-contractors under NEC ECS or NEC ECSS or a consultant under NEC PSC. The NEC TSC provides Employers the opportunity to engage suppliers for construction or non-construction on a term basis.

The pivotal role under the NEC ECC is the Project Manager, who is appointment by the Employer to administer the ECC to achieve the Employer's objectives.

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<sup>3</sup> quoted in Dr Arthur McInnes The New Engineering Contract: A Legal Commentary'

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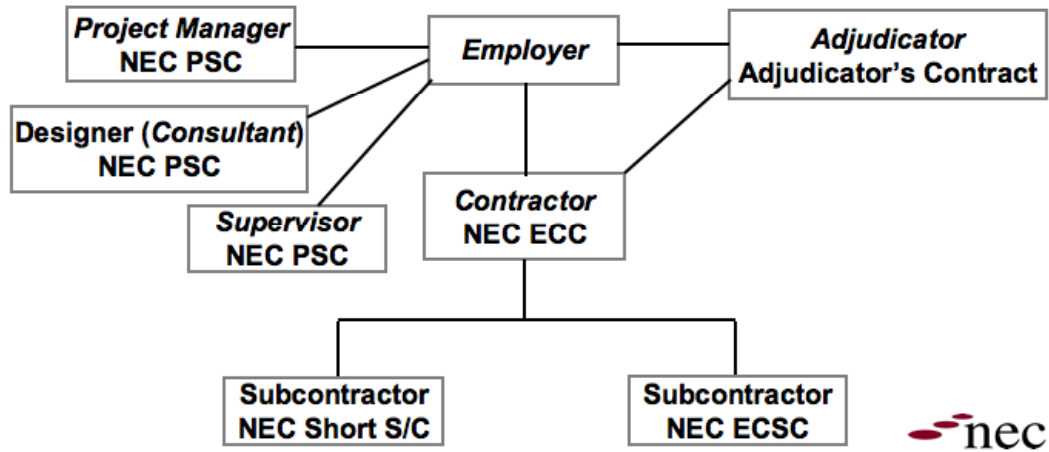


Figure 1: The NEC family: traditional bi-party partnering arrangement

This is a traditional arrangement where an independent designer designs the works and the Contractor is engaged to construct them. The Contractor can design some elements in this arrangement. This is a bi-party partnering arrangement.

Following on from figure 1, a bi-party partnering design and construct arrangement can be achieved where the Contractor who is engaged to construct the works is responsible for design. It is always open as to who fulfils the role of Supervisor (the person who's role is to check the quality of the works is in accordance with the contract). This could be an Employer appointment of an independent firm or even the Contractor can fulfil this so as to achieve a self-certification arrangement.

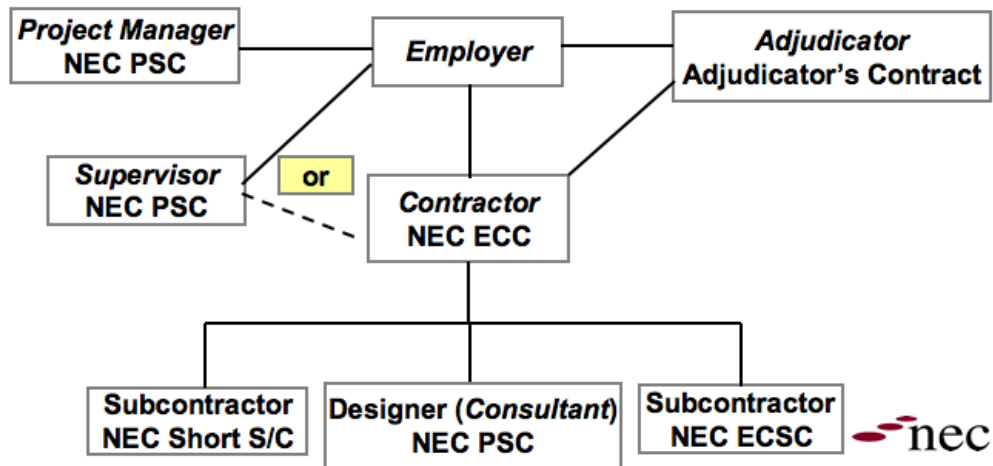


Figure 2: The NEC family: Design and build bi-party partnering arrangement

Figure 3 shows a traditional arrangement where the design of the works is carried out by an independent designer and the Contractor is engaged to construct the works but this time Partnering Option X12 is included in the contracts of key supply chain members. Again, an element of design can be carried out by the Contractor and in this arrangement, a multi-party partnering arrangement is achieved.

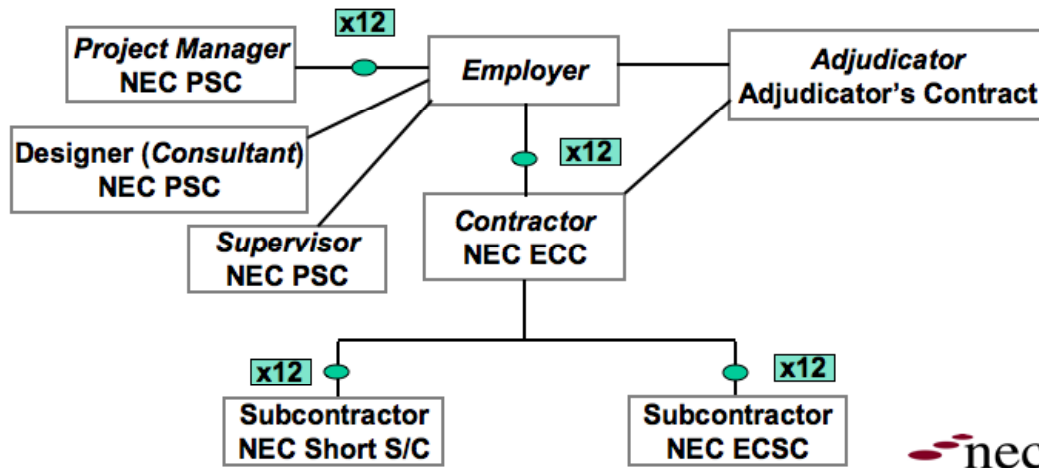


Figure 3: The NEC family: Multi-party partnering arrangement – NEC Partnering Option X12

NEC Partnering Option X12 creates an open structure and is the common link within suppliers' NEC contracts and creates the multi-party partnering arrangement. The benefits are that a Core Group is appointed from the selected suppliers pool to partner the project, not all suppliers have to be engaged from day 1 of the project, they can come and go to complement the project lifecycle and suppliers are comfortable in a bi-party relationship with the added benefit they can be aligned to project objectives through Key Performance Indicators.

A design and construct arrangement can be drawn from figure 3 using Option X12 and moving the designer to a sub-consultant of the Contractor.

### NEC Users' Group

The NEC has an active Users' Group that currently has some 250 members from across the industry with a remit to share best practice. It has regular newsletters, offers a member Helpline facility, hosts seminars, workshops and roadshows. More details can be found on [www.neccontract.com](http://www.neccontract.com).

## Key ECC Characteristics

### Actions

Clause 10.1 requires certain of the NEC players to 'act as stated in this contract and in a spirit of mutual trust and co-operation'. This is quite a departure from most conditions of contract and law, and covers both obligations and attitude.

### Communications

All communications under ECC must be in a form that can be read, copied and recorded. The Project Manager and Contractor must reply to communications within the period for reply.

### Project Manager

The Project Manager plays a pivotal role in administering ECC contracts.

- The Project Manager is the key management person on behalf of the Employer
- All Project Manager decisions should reflect the Employer's business decisions

- Any Project Manager acceptance of communications from the Contractor does not change the Contractor's responsibility to Provide the Works of his liability for his design
- It is essential that the Project Manager is sufficiently close to the work and has the time and authority to carry out his duties effectively
- The Contractor has recourse to an Adjudicator where he believes the Project Manager's actions or decisions do not accord with the ECC

### Early Warning

This is the jewel in the crown of the ECC. The Contractor and Project Manager both have a duty to notify each other if aware of a matter that could:

- increase the total of the Prices
- delay Completion or
- impair the performance of the works in use.

Once early warning is given, there is an instruction to attend meeting and those attending consider proposals, seek solutions and decide actions.

The focus of the meeting is to solve the problem in the interests of the project. It is about prevention rather than cure and focuses participants' efforts to be proactive rather than reactive. It encourages collaboration, innovation and ability to adjust to circumstances during the contract.

### Programme

The ECC relies upon an up-to-date and realistic programme being at the heart of management of the contract. The Accepted Programme is latest accepted by Project Manager and includes the likes of

- key dates
- method statement for each operation, and
- order and timing of operations.

It is therefore likely to be a collection of documents, which may include method statements, histograms, network diagrams, bar charts and the like. The frequent updating allows the best chance for foresight in resolving time and resources issues of change and problems to be understood and properly dealt with, with minimal waste occurring.

### Compensation events

Compensation events are events that, if they occur, and do not arise from the Contractor's fault, entitle the Contractor to be compensated for any effect the event has on the Prices and the Completion Date.

The compensation event process includes notification, quotation, assessment and implementation. The aim of compensation event assessment is to agree the whole cost and time implications that each event has, ideally using a resource forecast approach, rather than having regard to tender allowances or schedules of rates.

### Risk

The ECC contains typical risk allocation provisions in compensation events and Employer's risk, but of course each project has its' own risk profile. There is provision made to alter risk allocation pre-contract according to project risk register and any subsequent negotiations during the tender period. There is also provision made within the ECC to re-appraise risk allocation when quoting for effects of compensation events.

## Value engineering

Provision is made in ECC target cost contracts for value engineering initiatives from the Contractor.

## Payment

There are a variety of payment options available within ECC, of which one must be selected prior to tender stage. The main factor to be considered in making this choice is risk. The ECC places great emphasis on the parties controlling and forecasting out-turn cost.

## Disputes

The ECC uses adjudication as the first step in resolving disputes before arbitration or litigation commences, the focus is, however, dispute avoidance and not dispute resolution.

## NEC in Use

In the UK in particular the NEC is used across the construction sector in building, civil engineering, utilities and power. Some of the major projects NEC is used on includes BAA's Heathrow Terminal 5, Channel Tunnel Rail Link, the Eden project and the National Health Services' ProCure21 hospital building framework. Outside the UK, Eskom in South Africa is a major user.

Some notable NEC attributes to date:

- It has been used in more than 20 countries
- Though statistics are somewhat difficult to gather, the NEC has been used on over 45,000 projects of some £20bn+
- There is no substantive NEC case law
- The NEC is probably responsible for generating a new breed of modern day forms of contract
- It is rarely not used subsequently by clients
- The UK Government believe NEC to be reasonable 'Achieving Excellence' compliant

As we better appreciate that project management plays an essential role in contract administration, that participants appreciate the plain English drafting style in relational contracts and we move away from bespoke one-off conditions to a contract structure that offers the flexibility we need, then NEC is likely to become a leading standard form of contract for the World to embrace.