

## **Professional Services Contract (PSC)**

### **INTRODUCTION**

The Professional Services Contract (PSC) has been developed as part of the New Engineering Contract (NEC) system of contract documents. The PSC has been drafted with the same objectives as the NEC and has adopted clauses from the Engineering and Construction Contract (ECC) where they were considered to be appropriate for the appointment of a professional organisation or person.

The purpose of the document is to form a standard contract for the appointment of consultants providing professional services to be used in engineering and construction generally. It can be used for the appointment of a project manager or a supervisor under an NEC contract and also for the appointment of persons fulfilling other roles associated with construction contracts (such as a designer responsible either directly to the Employer or to the Contractor in a construction contract) or for appointments of consultants in advance of construction (e.g. appointment of a project manager or designer during the early development stages of a project).

Its use however is not limited to projects where other NEC contracts are being used. It can be used where no construction works are to take place or where other forms of contract for construction are being used. When the PSC is used by a contractor (for instance, to appoint a designer as a subcontractor in a "design and construct" contract) the contractor has the role of "Employer" in the PSC. In such circumstances, the PSC can be used as a subcontract (ECC clause 26.3) with appropriate amendments, (See Appendices 3 and 4)

The contract has been drafted as a 'shell' contract which requires important information to be provided separately. The most critical document to be provided is the Scope. This contains the detailed requirements of the Employer and is frequently referred to within the PSC.

The purpose of these guidance notes is to explain the reasons for some of the provisions in the PSC and to provide guidance on how to use it. Where clauses are similar to those in the Engineering and Construction Contract, reference may be made to the ECC Guidance Notes for further explanation. The flow charts show the procedural logic on which the PSC is based and are published in this volume for reference.

The NEC conventions of using italics for terms which are identified in the Contract Data and capital initials for terms defined in the PSC have been used in these guidance notes. Neither the guidance notes nor the flow charts are contract documents, nor are they part of the Professional Services Contract. They should not be used for legal interpretation of the meaning of the PSC.

### **CONTRACT STRATEGY**

The Employer chooses the contract strategy. This determines the specific professional services to be carried out, the basis of payment and the balance of risks between Employer and Consultant. The decision on contract strategy will identify the options from the Professional Services Contract to be chosen, the need for other provisions, and some of the material to appear in the Scope.

#### **The main options**

There are four types of payment mechanism available through the main options.

- Option A Priced contract with activity schedule
- Option C Target contract    Option E Time based contract
- Option G Term contract

For a particular contract, one main option must be chosen. The clauses from the selected main option are combined with the core clauses and the clauses from the selected secondary options to provide a complete contract.

The main options provide different allocations of risk between the Employer and the Consultant and use different arrangements for payment to the Consultant:

- Option A is a lump sum priced contract in which the risks of being able to Provide the Services at the agreed prices in the activity schedule are largely borne by the Consultant.
- Option C is a target contract in which the financial risks are shared by the Employer and the Consultant in agreed proportions.
- Option E is a type of cost reimbursable contract in which the financial risk is largely borne by the Employer.

- Option G is a term contract in which various items of work are priced or stated to be on a time basis. Thus the risk of being able to perform the instructed Tasks at the agreed prices or staff rates is largely borne by the Consultant, whilst the Employer retains control over the individual Tasks to be carried out.

The ad valorem or percentage fee type of contract has not been included as an option. Under this arrangement, payments to the Consultant are an agreed percentage of the works construction cost. This implies that the cost of the Consultant's services is proportional to the cost of constructing the works. Its merits were carefully considered, but rejected for the following reasons:

- the Consultant has no incentive to produce an economical design or other service.
- the cost of construction is largely a function of the market and bears no relation to the cost of professional services
- The final cost of construction (and therefore the final fee) is not established until after construction is complete, whilst most professional costs are expended much earlier and even before construction starts.
- the effect of variations to the Scope on the payments due to the Consultant are difficult to assess.

#### **Option A : Priced contract with activity schedule**

Under this contract the Consultant is paid a lump sum for the services. An activity schedule is a list of the activities which the Consultant expects to carry out in Providing the Services. When it has been prepared and priced by the Consultant, the lump sum for each activity is the price to be paid by the Employer for that activity. The total of these prices is the Consultant's lump sum price for providing the whole of the services.

#### **Option C : Target contract**

Target contracts are sometimes used where the extent of work to be done is not fully defined or where anticipated risks are greater. Although used frequently in construction contracts, they have had limited application in consultancy contracts. The financial risk is shared between the Consultant and the Employer in the following way.

- The Consultant tenders a target price in the form of a priced activity schedule. The target price is the Consultant's estimate of Providing the Services and is defined as the total of the Prices
- The Consultant tenders his staff rates
- During the course of the contract the Consultant is paid the Time Charge which is the staff time for the services carried out priced at the appropriate staff rates. This is defined as the Price for Services Provided to Date
- At the end of the contract, if the final Price for Services Provided to Date is less than the final total of the Prices, the Consultant is paid his share of the difference according to the formula stated in the Contract Data. If the final Price for Services Provided to Date is greater than the final total of the Prices, the Consultant pays his share of the difference.
- The Scope must be sufficiently descriptive to enable the Consultant to price the services in his tender.
- The target price set at the Contract Date may change during the contract as the compensation events procedure is applied to changes in the Scope and other compensation events.

#### **Option E : Time based contract**

This is a cost reimbursable type of contract which should be used when the services cannot be defined sufficiently accurately for a lump sum to be quoted. In such circumstances the Consultant cannot be expected to take cost risks other than those which the control of his employees and other resources entails. He carries minimum risk and is paid the Time Charge (as defined by the staff rates stated in the contract).

#### **Option G : Term contract**

This contract provides for the appointment of a Consultant for a term (an agreed period of time). The Consultant prices a task schedule prepared in advance by the Employer as well as providing staff rates for different grades of staff. Each price on the task schedule is a lump sum for that particular item. Some items on the task schedule may be stated to be carried out on a time basis rather than for a lump sum price.

When the Employer requires specific services to be carried out by the Consultant he identifies a proposed Task by selecting individual items from the task schedule. Any items not on the task schedule are notified as compensation events and the compensation event assessment procedure is

used to determine how each item is to be paid for. The Consultant carries out each Task only when he has been instructed to do so by the Employer.

### **The secondary options**

After deciding the main option, the Employer may choose any of the secondary options which are:

- Option X1: Price adjustment for inflation
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- Option X2 Changes in the law
- Option X3 Multiple currencies (used only with Options A and G)
- Option X4 Parent company guarantee
- Option X5 Sectional Completion (not used with Option G)
- Option X6 Bonus for early Completion (not used with Option G)
- Option X7 Delay damages (not used with Option G)
- Option X8 Collateral warranty agreements
- Option X9 Transfer of rights
- Option X10 Employer's Agent
- Option X11 Termination by the Employer
- Option Y(UK)1 The Construction (Design and Management) Regulations 1994 Option Y(UK)2 The Housing Grants, Construction and Regeneration Act 1996
- Option Z Additional conditions of contract

Any combination of secondary options may be used.

The Trust Fund secondary option included in the Engineering and Construction Contract has not been included in the PSC since the use of such an option in a contract for professional services is much less likely than in the case of a construction contract. If an Employer wishes to include such an option, the Trust Fund Option in the ECC should be used as a basis.

### **OptionX1: Price adjustment for inflation**

This option should be used if the Employer decides to accept the risk of inflation.

The price adjustment factor (PAF) is calculated on each anniversary of the Contract Date (cl XI.1) and is then used during the following year to make adjustments for inflation.

The Employer decides which published index to use, eg the Retail Price Index, and enters this in Part one of the Contract Data.

The Consultant's staff rates stated in Part two of the Contract Data may be either

- fixed, and thus not variable with changes in salary actually paid to individuals or
- variable with changes in salary paid to individuals

### **Fixed staff rates**

In all the main options, an amount for price adjustment is calculated as stated in clauses XI.1 and XI.2 and for expenses adjustment in clause XI.6.

As the adjustment amounts are recorded separately in the amount due, in a target contract (Option C) the Price for Services Provided to Date continues to be comparable to the Prices (the target) for the purpose of calculating the Consultant's share.

**Variable staff rates** Different clauses are used according to which main option applies, as follows:

- Option A Clauses X 1 . 1 XI. 2 XI. 5 X1.6
- Option C Clauses XI.1 XI.3 XI. 5 XI. 6
- Option E Clause XI. 6
- Option G Clauses XI-1 XI.4 X1.5 XI. 6

For a priced contract using an activity schedule (Option A), an amount for price adjustment is calculated as stated in clauses XI.1 and XI.2. The Time Charge to be used in the assessment of compensation events is adjusted to the Contract Date using clause XI.5 in order to maintain the time basis of the Prices.

For target contracts (Option C), an amount for price adjustment is added to the Prices (cl XI.3) so that the total of the Prices can be fairly compared with the final Price for Services Provided to Date (the Time Charge using variable staff rates) for calculating the Consultant's share. The Time Charge to be used in the assessment of compensation events is adjusted to the Contract Date using clause XI.5.

For term contracts (Option G), a price adjustment is necessary only for the lump sum items in the task schedule using clause XI.4. The Time Charge to be used in the assessment of compensation events (including the lump sum items added to the task schedule under clause 55.1) is adjusted to the Contract Date using clause XI.5.

For all the main options (Options A, C, E and G), if the expenses are stated in the Contract Data as fixed prices and are not adjustable for inflation, an amount for expenses adjustment should be included in the amount due in accordance with clause XI.6.

Worked examples of the calculations of the amounts for price adjustment and expenses adjustment are given in Table 1.

#### **Option X2 ; Changes in the law X2.1**

This option reduces the effect on the Consultant's costs and programme of the risk of changes to an applicable law which occurs after the Contract Date by making such a change a compensation event. Such changes can have a dramatic effect on the Consultant's costs and his liability to make progress on the services.

The Employer should review the laws which could be relevant to the services and identify those where he is prepared to carry the risk of changes as applicable law in the Contract Data. These could be the law of the contract (cl 12.2), the law of the country where the services are to be provided, where the construction site is or where a major supplier is located.

For the purposes of this clause, the law includes a national or state statute, ordinance, decree, regulation (including building or safety regulations), by-law of a local or other duly constituted authority and other delegated legislation.

#### **Option X3: Multiple currencies ( used only with Options A & G) X3.1**

This option is used (in conjunction with main options A and G only) when it is intended that payment to the Consultant should be made in more than one currency and that the risk of changes in the exchange rates should be carried by the Employer.

The Employer should state in the Contract Data which items of work are to be paid for in currencies other than the currency of this contract, what those currencies are, the maximum amounts payable in each currency and the exchange rates to be used in calculating the payments. Exchange rates are usually those published some two weeks before the Consultant submits his offer to the Employer. Any subsequent movement of the exchange rates is therefore at the Employer's risk. No provision is made for multiple currencies in main Options C and E because the Consultant is paid the Time Charge.

#### **Option X4: Parent company guarantee X4.1**

This option should be included where the Employer requires the greater security provided by the parent company for the performance of the Consultant.

#### **Option X5: Sectional Completion (not used with Option G) X5.1**

This option should be included when the Employer requires parts of the services to be completed by key dates before the whole of the services. The parts are called sections each of which should be identified in the Contract Data part one, with a completion date for each. Completion of the sections is followed by Completion of the whole of the services. The sections do not make up the whole of the

services but establish key dates. Delay damages and bonus for early completion can be related to section completion dates by using Options X7 and X6 respectively.

#### **Option X6: Bonus for early Completion (not used with Option G)X6.1**

Where Completion as early as possible would benefit the Employer, whether of all or a section of the services, the Employer can use this Option to achieve early Completion. The bonus calculated in accordance with this clause will be included in the assessment occurring at Completion of the whole (or section) of the services.

#### **Option X7: Delay damages (not used with Option G)X7.1**

Delay damages are the liquidated damages paid by the Consultant when he fails to complete the services (or sections of the services if option X5 is also used) by the Completion Date. Under English law and some other legal systems, if it is not included, delay damages are "at large" and the remedy open to the Employer is to bring an action for damages for the Consultant's, breach of contract. In this event, evidence of the actual damage suffered by the Employer is required.

The amount of delay damages should not exceed a genuine pre-estimate of the damage which will be suffered as a result of the Consultant's, breach. They are described as delay damages because these are not the only liquidated damages in the PSC. Interest on late payments as provided for in clause 51.4 is a form of liquidated damages.

Appropriate entries for delay damages should be made in the Contract Data. They may represent cost to the Employer caused by delayed start to another contract, or simply interest on the capital invested in the services of which the Employer has been deprived of the benefit. Damages greater than a genuine pre-estimate constitute a penalty and are not generally enforceable under English law.

Since delay damages are amounts to be paid by the Consultant, appropriate deductions are made in the first assessment of the amount due, occurring after the Completion Date, and in subsequent assessments up to Completion.

X7.2 This clause protects the Consultant when he has paid delay damages and a later assessment of compensation events results in a delay to the Completion Date. This could arise when a compensation event occurs at a late stage or if an Adjudicator or tribunal changes the assessment of a compensation event, and the decision is made after delay damages have been paid.

#### **Option X8: Collateral warranty agreements X8.1**

A collateral warranty agreement is an agreement entered into by the Consultant with purchasers or tenants or funding organisations (who are not the Employer) of an industrial or commercial development. It has the effect of binding the Consultant in contract, and creating legal liability toward parties Other than the Employer which may not otherwise exist. Details of the collateral warranty agreements which the Consultant will be required to enter into should be stated in the Contract Data.

These details should include

- form of warranty agreement
- limitation period
- insurance requirements
- rights of assignment, including number of assignments to subsequent purchasers/tenants, permitted
- others providing warranty agreements

A requirement to enter into such agreements can represent a considerable extension of a Consultant's liability. Legal advice may be necessary and advisable. The British Property Federation has published model forms of collateral warranty which have been agreed by the ACE, RIAS, RIBA and RICS, after consultation with the Association of British Insurers.

#### **Option X9 : Transfer of rights X9.1, X9.2**

The rights over drawings, documents, designs and the like prepared by the Consultant would normally remain with the Consultant. The core clauses recognise this but give the Employer

entitlement to use any documents for the purposes stated in the Scope. If, in addition to this, the Employer wishes to obtain the rights for himself, this option should be chosen. The option permits the Consultant to use designs and documents for other work subject to restrictions and obligations set out by the Employer in the Scope.

#### **Option X10 : Employer's Agent X10.1**

This option should be used where a corporate body wishes to appoint an individual, either from within its own organisation or an external consultant, to act as its agent under this contract. The Agent should be identified and the extent of the Agent's authority defined in the Contract Data.

#### **Option X11 : Termination by the Employer XII.I,XI 1.2**

Under the core clauses the Employer is entitled to terminate following the substantial failure of the Consultant to carry out his obligations, on insolvency of the Consultant, or when the Employer no longer requires the services. This option gives a further power to the Employer to terminate the appointment of the Consultant for a reason not stated in the contract which might involve no default of the Consultant.

This clause gives the Consultant entitlement to increased payment if the Employer terminates for a reason not stated in the contract. The 5% payment is arbitrary, but recognises that the Consultant has been deprived of some profit which he would have made if he had been permitted to continue with, and complete, the services.

#### **Option Y(UK)1: The Construction (Design and Management Regulation 1994)**

These regulations apply to the majority of construction work carried out in the United Kingdom. Hence this option should be used wherever the regulations apply to the Consultant's work. For each project a planning supervisor and a principal contractor are appointed with extensive powers to manage health safety and welfare at the design stage and throughout construction on site. Thus a Consultant doing design work or site supervision may be affected by the regulations.

The duties and powers of all parties involved in a project are set out in (the regulations and are not repeated in the contract. This optional clause deals with payment arising from application of the regulations. The financial risk is shared between the Employer and the Consultant, the dividing line being based on what an experienced consultant could reasonably be expected to have foreseen.

#### **Option Y(UK)2: The Housing Grants, Construction and Regeneration Act 1996**

This option is prepared solely for use on contracts which are subject to The United Kingdom Housing Grants, Construction and Regeneration Act 1996 Part II ("the Act"). The option should not be used in other circumstances.

The (two principles contained in this Act. which affect the NEC Professional Services Contract, are those related to payment and adjudication. The definition of a "construction contract" in this Act is wide ranging and can be found in Section 104. It covers not only an agreement to carry out "construction operations" but also "an agreement to do architectural, design or surveying work, or to provide advice on building, engineering, interior or exterior decoration or on the laying-out of landscape in relation to construction operations". Thus the Act will apply to many agreements made using the Professional Services Contract.

The definition of a "construction operation" can be found in Section 105(1) of the Act. The operations and contracts that are not subject to the Act are defined in Sections 105(2) and 106. In the United Kingdom (England, Wales, Scotland and Northern Ireland), the Parties to a contract should consider carefully whether the operation is subject to the Act before proceeding. If the operation or contract is subject to the Act, it is intended that, by incorporating Option Y(UK)2 into the contract, the provisions of the statutory Scheme for Construction Contracts do not become implied terms of the contract [S. 114(4)]. Parties must be aware that it is not possible to contract out of a statutory requirement.

Clause Y2.1 deals with the measurement of time periods in relation to the Act. Clauses Y2.2 to 2.4 and clause Y2.7 have been drafted with the intention of complying with Sections 109 to 113 and clauses Y2.5 and 2.6 have been drafted with the intention of complying with Section 108 of the Act.

In the NEC family of contracts periods of time are usually measured in weeks thus avoiding complications of rest days and statutory holidays in different countries in which these contracts are

used. The Act, however, defines most periods as a number of days. S.I 16(3) of the Act states that Christmas Day, Good Friday and bank holidays are excluded from any period specified in the Act. Where the time period associated with the Act is referred to, that period has been stated in days in Option Y(UK)2.

The key periods affecting the procedure for payments when Option Y(UK)2 applies are illustrated in Figure 1 which includes references to the Act and to the Y(UK)2 clauses. Figure 1 should be referred to in conjunction with the following notes on clauses Y2.2 to Y2.4.

Y2.2. 2.3 and 2.7 These replacement and additional clauses in Y(UK)2 are drafted to accommodate Sections 109 to 111 of the Act. The Employer is now required to give notice to the Consultant of the payment to be made, and the basis on which the calculation is made. This is achieved by the replacement clause 51.1 in conjunction with the first bullet of additional clause 56.1.

It should be noted that core clauses 51.2 to 51.5 remain in place. In particular, clause 51.3 deals with disagreement with the assessment of an invoice whereas the Act [S.I 16(2)] deals with set-off or abatement which Y2.3 provides for in the additional clause 56.2.

The Act uses very specific language about what and when "payments become due", when particular notices are issued and defining the "final date for payment". The latter applies to each certified payment and not just to the final payment "after Completion of the whole of the services". Provision has been made for a different payment period to be stated in the Contract Data (reference replacement optional statement in Y2.7).

The additional clause 56.1 sets out time periods and circumstances to meet the requirements of S. 110 (1) and 110(2) of the Act. S. 110(1)(a) requires an "adequate mechanism for determining what payments become due under the contract and when". This mechanism is provided by the Employer's certificate which is required to be issued by the date when payment becomes due (cl 51.1) which is 7 days after the assessment date (cl 56.1. 2nd bullet). S. 110(1)(b) requires that there should be "a final date for payment in relation to any sum which becomes due". This is 21 days, or the period stated in the Contract Data, after the date on which payment becomes due (cl 56.1 third bullet). The significance of the final date for payment is that if the Employer intends to withhold part of the amount due, he must give notice not later than a "prescribed period" ie 7 days before the final date for payment as indicated in S. 111 of the Act (cl 56.2).

Y2.4 Under S.I 12 of the Act. where a sum due is not paid by the final date for payment and no effective notice to withhold payment has been given, the Consultant has a right to suspend performance. This right can only be exercised if the Consultant gives 7 days' notice of his intention. The right to suspend ceases when payment is made in full. Under S. 112(4) of the Act. the Completion Date is, in effect, delayed by the period of suspension. The effect of the additional clause 604 is to treat such suspension as a compensation event. Thus, in addition to the extra time, the Consultant is entitled to additional costs resulting from the suspension.

The provisions in the Professional Services Contract for settling disputes do not comply with the Act although the principle of independent adjudication has been a key feature of the NEC family since its first publication in 1991. The purpose of Section 9 has always been to overcome where possible the causes of disputes and, in those cases where disputes may still arise, to facilitate their clear definition and early resolution. Hence this amendment replaces core clause 90 with new clauses which should comply with the Act. The intention of the new clauses is to retain the principles of the adjudication provisions in the PSC in managing disputes, and at the same time comply with the Act so that the fall-back "Scheme for Construction Contracts" does not apply.

Figure 2 should be referred to in conjunction with the notes on clauses Y2.5 and Y2.6.

The new clauses require a meeting to be held to discuss any matter of dissatisfaction, with a view to resolving the matter. If this procedure fails to resolve the matter, a dispute arises after which either Party can give notice of his intention to refer it to adjudication. The remaining procedure in the clause is similar to that in core clause 90.

Y2.6 Y(UK)2 clause 90 supersedes core clause 91.1 which is deleted. The new clause 91.1 extends the procedure for a meeting to resolve a matter of dissatisfaction, to include a subcontractor, where the relevant matter is one which involves the subcontractor. The new clause 91.3 requires the Consultant who is a subcontractor under the PSC to attend a meeting of the main contract parties, which is held to deal with a matter of dissatisfaction common to both contract and subcontract. Core clauses 91.2 and 91.3 are retained, but the latter has been renumbered 91.4.

**Option Z: Additional conditions of contract** This option should be used where the Employer wishes to include additional conditions. These should be carefully drafted in the same style as the core and option clauses using the same defined terms and other terminology. They should be carefully checked for consistency with the other conditions.

Additional conditions should be used only when absolutely necessary to accommodate particular needs, such as those peculiar to the country in which the work is to be done. The flexibility of the PSC main and secondary options minimises the need for additional conditions. Additional conditions should not be used to limit how the Consultant is to do the work in the contract as this is part of the function of the Scope.