

Webinar: Assuring Plant, Material and Equipment Costs under NEC4

Q&A

Please note all responses are provided based on an unamended NEC4 Engineering and Construction Contract (ECC).

In the railway environment, it is common that only 4-5 hours per night are available due to Client restrictions on access. Equipment providers (e.g. Road Rail Vehicles) are usually charging the contractor a minimum 8 hours for hire of the RRV. What would be the correct Defined Cost for the Contractor? The Equipment is only "Providing the Works" for max 5 hours, however the open market for these RRVs all charge minimum 8 hours?

A: In the Schedule of Cost Components, cost component 21, 22 and 23 all refer to “the time for which Equipment is required”. If the Equipment is required for 8 hours i.e. the duration of the shift, then it will be the 8 hours that will be due for payment. This will also be evidenced by the amount the *Contractor* has to pay to hire the Equipment. This is in part confirmed by clause 11.2(26) Disallowed Cost which states that a Disallowed Cost includes “resources not used to Provide the Works (after allowing for reasonable availability and utilisation) or not taken away from the Working Areas when the *Project Manager* requested”. In this case the difference between the 8 hour charge and the 5 hours working period should be considered as “reasonable availability and utilisation” as on any construction site many items of Equipment will not be working 100% of the time.

Since the advent of COVID and the norm is now very much working remotely, what would be acceptable as the working area?

A: The Working Areas are defined in clause 11.2(20), which sets out the criteria that the area must meet for it to be considered a Working Area. In particular the area must be “used only for work in the contract”. A home would not fulfil this criterion as it is used for other purposes. To address this issue, the January 2023 amendments introduced a further category of people whose costs could be recovered by the *Contractor* even if their normal place of working is outside the Working Areas and they are working outside the Working Areas, for example working from home. However, these people must be listed in Contract Data part two.

In the ECC Option F (not widely used I understand), there is no Short or Schedule of Cost Components in the CD2, thus in terms of 52.1, you would see Defined Cost as other amounts at open market or competitively tendered prices with deductions for all discounts, rebates and taxes which can be recovered or what other method do you use to audit the Contractors costs to determine Defined Cost [11.2(25)]?

A: Under main Option F the *Contractor* will engage Subcontractors to deliver the *works*. If the *Contractor* undertakes any work itself, it will recover the cost of that work using *prices* stated in Contract Data part two (clause 11.2(25)). The costs of any Subcontractors will need to comply with the requirements stated in clause 52.1 and therefore be at an “open market or competitively tendered prices with deductions for all discounts, rebates and taxes which can be recovered” as you have identified in your question. The *Contractor* will have to provide access to accounts and records in relation to Subcontractor costs in accordance with clause 52.3 to demonstrate this.

Would a Subcontractor have to demonstrate that sub sub contractors defined cost are competitive?

A: The ECC only requires the *Contractor* to comply with clause 52.1 in relation to its Subcontractors and suppliers. The *Project Manager* does not have access to or visibility over sub-subcontractors. However, in order to determine whether a cost should be considered a Disallowed Cost under the bullet point “cost which should not have been paid to a Subcontractor or supplier in accordance with its contract” the *Project Manager* may need to review the amounts paid by the *Contractor* to a Subcontractor in regards to costs the Subcontractor has paid to its subcontractors or suppliers if the Subcontractor is engaged under a cost reimbursable form of NEC subcontract by the *Contractor*.

I've encountered a situation recently whereby rates for people and equipment have been included in CD, however, it also states that the rates are subject to audit. This appears to defeat the objective of having pre-agreed rates in the CD. If rates have been benchmarked in advance to demonstrate value for money, should or would there be a need to also audit the rates?

A: The amounts payable as Defined Cost will be as stated in the relevant schedule of cost components. This will either be a rate or percentages stated in Contract Data part two or actual cost. An audit will only be required of those costs paid on an actual cost basis. The requirement in clause 52.1 to demonstrate that rates and prices are “at open market or competitively tendered prices with deductions for all discounts, rebates and taxes which can be recovered” only applies to costs paid on an actual cost basis and not those for which rates have been stated in Contract Data part two. Any requirements to the contrary would need to be included as a Z clause amendment. We have seen this occasionally as a Z clause amendment and it may be the rates weren’t tendered or benchmarked, so the *Client* has taken them initially on good faith. The audit will prove their accuracy (they could be more or less) and from there on in the “audited” rates become the basis for reimbursement.

On an Option E contract, a number of equipment costs were paid (such as stationary) incorrectly, do I have grounds to now disallow even though they have been paid?

A: Under the ECC each payment is cumulative and therefore the assessment of Defined Cost, and as part of this Disallowed Cost, can be revised until Defined Cost has been finalised either under clause 50.9 or 53.1

When using rates for equipment over a long period, do we need to include a z clause to allow these to be amended over the course of the contract to reflect market adjustments over time?

A: If rates and percentages have been included in Contract Data part two, these are fixed for the duration of the contract.

Which evidence do you recommend between invoice & receipt in relation to final account audit?

A: Evidence should always start with invoice and proof of payment. Knowledge and understanding of the works and regular physical inspections of the Site may mean there is no further requirement for the *Project Manager* to request additional records, as you have assured yourself of physical incorporation of the Plant and Materials into the works. However, if either the invoice description is vague or the *Project Manager* is remote from the works then proof of delivery and/or purchase order and/or requisition order may be valid accounting records to request.

Are Weekly labour and equipment returns demonstrating use within working areas even more important now to demonstrate the Contractors application even though it might be open book contracts?

A: Labour and Equipment returns are excellent and important site records which add further evidence beyond accounting records that resources have been allocated correctly in Providing the Works. They give an extra layer of detail aligning resources to specific tasks and activities. Some accounting systems may capture this level of detail but this is relatively rare.

Is it reasonable to request that the contractor provides site contemporaneous records to review against duly authorised timesheets to validate time spent providing the works? I've often encountered instances where timesheets don't appear to have been checked correctly before being authorised.

A: The requirement for these contemporaneous records could be included in the Scope. We regularly see these added as do we see the requirements for timesheets to be submitted weekly, with appropriate level of authorisation from *Contractor* and / or *Project Manager* being required to facilitate payment.

When looking at equipment rates in NEC, it often notes CECA rates. ahead of the rates pages, there are some notes (Section A and Section B). Are these notes relevant under NEC? There is a conflict of terms i.e notably Section B asks for invoice amount plus a % for items hired in for dayworks, however, "Dayworks" is not a concept in NEC

A: When rates are added (CECA or other) it is essential to confirm the specific guidance relating to charging terms or rules that accompany these rates. This avoids dispute at a later day.

I have the project commercial team assessing option C AFP, suggesting that for equipment cost, the delivery note plus the bank transaction record would be sufficient for validating

the cost. The inspection on site for equipment utilisation and the site progress would not be necessary because they assess the payment base on actual cost instead of progress.

What is your view on this argument?

A: For Equipment, it is the on hire and off hire notes, not delivery notes that drive charging within the accounting system. Invoice and payment checks are always a good place to officially start as they validate the cost. However, this does not prove full entitlement as the Equipment may have been idle and could be subject to Disallowed Cost. So, Equipment utilisation and progress reports are valuable information sources to cross check the period of charging against.

In checking time sheets, do we also check whether the time spent is reasonable in order to Provide the Works? In case of dispute between the PM and the Contractor on 'reasonable time', what is the yardstick in deciding 'reasonable' time?

A: Under main Options C to D of the ECC, the definition of Defined Cost is the cost of the components in the Schedule of Cost Components less Disallowed Cost (clause 11.2(24)). Disallowed Cost is defined in clause 11.2(26) and includes the bullet point “the cost of resources not used to Provide the Works (after allowing for reasonable availability and utilisation) or not taken away from the Working Areas when the *Project Manager* requested.”

In order for this bullet to apply the resource, which includes people, will have to not be working as opposed to working inefficiently. This will be a decision for the *Project Manager* to make based on the specific facts of the matter.

Bottom line of Darren's second last slide relates to Disallowed Cost for Defects caused by the Contractor not complying with a constraint on how it is to Provide the Works stated in the Scope. The user guide mentioned that this is about method, and a wrong location of the works is not 'how'. Is this correct?

A: Yes, the NEC4 User Guide is correct.

Slight topic tangent. A main contractor is working on an NEC4 option C contract upstream. There are some subcontractors on contracts where retention is being withheld. In terms of the upstream AFP, should the contractor be paid the gross certification amount of a subcontractor or the net amount after retention has been deducted?

A: In an NEC4 Engineering and Construction Contract, Schedule of Cost Components, cost component 41 payments to Subcontractors should not take “into account any amounts paid to or retained from the Subcontractor by the *Contractor*, which would result in the *Client* paying or retaining the amount twice.” In a situation where there is retention under the main contract the amount payable to the *Contractor* for their Subcontractors would exclude retention, as if not retention would be retained by the *Client* twice, at the main contract and subcontract level. If however, there is no retention at the main contract level the *Client* would pay to the *Contractor* the amounts the *Contractor* has paid to the Subcontractor after retention has been removed by the *Contractor*. As in this case retention would only be deducted once.

Where rebates occur that are linked to a Contractor's overall turnover with a Supplier, 1) can these rebates be applied to your contract if they are not contract specific 2) how do you practically apportion the rebate to your contract?

A: In accordance with clause 52.1 of the ECC, the *Contractor* should make “deductions for all discounts, rebates and taxes which can be recovered”. This would apply to discounts and rebates received at a contract or corporate level. The *Contractor* should make the *Project Manager* aware of any such discounts and rebates and agree a reasonable method for apportioning the cost of the discounts and rebates applicable to the amount of Equipment and Plant and Materials used on the contract that are the subject of the discounts and rebate.

In the example the cost ledger show 14,592 records, was this Contractor information overload? Or using common sense could this be simplified for AfP'S?

A: This was how the data came out of the *Contractor's* accounting system and was not there to confuse the *Project Manager*. All accounting systems work slightly differently. In this case the costs were captured on receipt of a Purchase Order on a line by line item basis. As mentioned in the webinar, another contractor with a different accounting system might only record costs on an invoice received basis. In such a case the volume of transactions would have been significantly fewer.