

## NEC IN AN INTERNATIONAL CONTEXT

While there are various forms of construction contracts that are used internationally, it is important to recognise that there is no single standard form that can be used in any jurisdiction regardless of the applicable governing law. A good form of contract however is drafted to provide for the flexibility to allow that contract to be used internationally and take account not only of legal requirements but also ease of use for construction professionals. This note therefore examines how the NEC form of contract can be used internationally and the benefits of using that form in an international context.

Looking first at the issue of the applicable governing law, or any other changes which may be required to comply for example with the local legislation where the project is located, this is provided for specifically through the Y clauses which can be used to address such issues. By keeping such amendments within an identified part of the contract, it is clear which provisions are only required for that reason and may not be required on other projects. In the UK this is used to deal with the requirements of the Construction Act but in other jurisdictions such as Australia it is used to deal with the Security of Payment legislation (which is different in all 7 states and territories). In South Africa, however, there are no Y Clauses and local users tend to use Option Z clauses even for matters such as local empowerment and local content (which might lend themselves to Y Clause arrangements).

It is however important to recognise that even in areas where no amendments are necessary, the governing law may mean certain provisions are interpreted or enforced in different ways. This is for example the case for liquidated damages, which are treated differently under common law and civil law systems or the ways in which different legal systems approach the interpretation of contracts.

The next important area is ease of use and clarity as to what is required. Contracts should be designed so that they can be used by the project team without the need for legal advice and in that respect the use of plain English and the concise nature of the drafting make the NEC form more accessible for users even in non English speaking countries. The other benefit of that style of drafting is that where translations are required because of legal requirements or because a language other than English is being used, the NEC forms of contract are easier to translate (subject to permission granted by NEC).

The other factor that affects the use of construction contracts is awareness of their terms and their use internationally. The NEC form of contract was first used in the UK and continues to be used on some of the largest mega projects such as Crossrail and Hinkley Point but it has an impressive track record of being used internationally, with places such as South Africa and Hong Kong being early adopters but NEC being used also in Australia (where Sydney Water chose to use NEC4 for its new procurement strategy and Main Roads Western Australia successfully trialling NEC), Europe (on projects such as the Luas Cross City line utility diversion works in Dublin, Ireland and the International Criminal Court Permanent Premises in the Netherlands) and more recently in South America where it was used when procuring venues for the Lima 2019 Pan American and Parapan American Games and in Belgium where it was used for the construction of a £3bn ring road (a dual carriageway including tunnels and elevated sections) in Antwerp by Lantis, the Flemish government company responsible for mobility infrastructure.

Overall, the growing use of NEC in various jurisdictions shows its suitability for international use. Looking more closely at some of the features that NEC offers demonstrates some of the benefits that it can bring to such projects. Key procurement influencers such as development funding institutions and commercial lenders, tend to focus on models which appear to provide cost and

time certainty, but often fail to do so, and need to recognise that the NEC's collaborative stance and fair approach to risk allocation is better suited to delivering such certainty in the long term.

## **Project Management**

Traditional forms of construction contracts tend to set out the parties' rights and liabilities in order to identify the consequences of failure so as to provide certainty in the event of a dispute between the parties. NEC also identifies the parties' rights and obligations but is different by putting an emphasis on creating processes that would result in pro-active project management, thereby leading to a successful outcome in terms of cost, time and quality.

This is evident from the way NEC manages communications, where it specifies periods for response in different circumstances as well as providing for deemed acceptances where a party fails to communicate. This encourages communications, to avoid delay in resolution. In particular, the early warning process and the use of the early warning register help ensure that risks are identified in advance and where possible their impact is avoided or reduced, which benefits both parties, as opposed to dealing with the consequences of risks that have materialised which often leads to disputes.

Another key benefit of using NEC is the way the programme is used as a joint project management tool. It is not unusual to find on projects parties using different versions of a programme for different purposes or allowing a programme to go out of date when the focus is solely on delivery. The NEC approach is different by, first, requiring the programme to be updated and accepted on a regular basis, and, second, by requiring the programme not only to be detailed but also include what is required from both the contractor and the client, as well as any other parties whose role will affect the progress of the works.

Looking at the early warning register and the programme together, if both those processes are followed then the programme will help identify the potential impact of risks in advance but also provide a reliable indication of the impact of any steps taken to manage those risks. It is difficult to see how a project can be well managed without the benefit of a comprehensive and updated programme and this is what the NEC seeks to achieve.

## **Better commercial management**

The importance of good commercial management can never be overstated and many international projects are funded by public bodies and international development banks that are keen to ensure that there is transparency of the costs being incurred as well as certainty on the final cost and full justification in the event that costs are increased. With traditional forms of contract, there is a tendency to leave any disputes until the works are complete and the actual cost is often not known until the final account process has come to an end, which often involves arbitration. As a result, it is often the case that only a few years after the works are complete that the client knows the full costs and, equally, the contractor will know whether it has suffered a loss or made a profit.

NEC addresses these concerns and provides different payment options, including a lump sum contract in countries where this is the accepted model and there is less experience with target cost contracts.

Where NEC has a real advantage is in how it manages changes as well as other risk events (compensation events) that lead to additional entitlement, in order to provide certainty and transparency. In that regard, NEC is different from other forms because all the compensation events are identified in one part of the contract and deal with both the time and cost impact. That is a clearer and simpler mechanism to operate which helps achieve certainty, especially as it is intended to work on an open book basis.

In addition, once the compensation events are identified, the contractual procedure provides for assessment within a short period which is based on the impact on the costs of providing the

works, which will usually be done as a forecast. The forecast once implemented is not changed later to reflect the actual cost impact. Similarly, the time impact is assessed at the same time, based on the updated programme which is managed by both parties. This means the costs to complete a project will be updated regularly and reliably, which allows the client to take proactive steps if, for example, it becomes clear that a budget will be exceeded.

When operated on that basis, the cost and time impact of compensation events should become clear contemporaneously as and when the works progress, promoting certainty and avoiding a situation where the full impact is only identified at the end. NEC does include a process for final assessment but it should be a more limited exercise if the majority if not all issues are determined in advance on the work proceeding and, in any event, it provides for fixed and relatively short periods for the final statement to be determined.

### **Collaborative Contracting**

Project management and commercial issues can lead to disputes and NEC was created in order to try to avoid some of the traditional adversarial behaviours that are found in construction projects by creating a more collaborative relationship. The detrimental impact of adversarial behaviours and the disputes and wasted costs that they create is of course not an issue that is limited to the UK and some of the ways to avoid such issues, such as the use of alliancing contracts, have originated and been used outside the UK.

As a result, there is a growing recognition internationally that disputes affect successful delivery and result in unnecessary costs and that modern procurement requires collaborative contracting. Indeed, there is a view that compared to the UK, other cultures have a stronger preference for resolving disputes through negotiation and relying instead on relationships, which makes collaboration even more appropriate.

This is something that NEC is very well suited for, having been designed from the outset as a collaborative contract which is based on open communications and a proactive management of risk. This is dealt with below but the key challenge for a successful collaboration is recognising that the commercial basis for the contract plays a critical role and that it is necessary to align the parties' interests and manage the commercial terms so they encourage rather than hinder collaboration.

One of the distinguishing features of the NEC form of contract is the ability to choose one of six payment options. This provides flexibility as to the commercial bargain but when it comes to collaboration and aligning the interests of the parties, this can be done through the use of Options C and D which create a target cost contract. While some clients may prefer a more traditional lump sum approach (Options A and B) the simple underlying principle of a target cost contract is that both client and contractor benefit from being able to reduce the costs of the project and have an interest in avoiding cost overspend. That encourages open and early communications about costs but also discussions that focus on the risks that affect projects and how to reduce or avoid the cost impact of such risks. This is of course very different from a traditional approach which focuses on which party bears any specific risk and therefore the sole responsibility for any resulting costs.

The other way in which NEC provides a balanced commercial basis is by taking a more flexible approach to the management of risk through the use of its optional X clauses. By requiring parties to consider which options should be used, as opposed to having them as a fixed part of the contract, this promotes a discussion as to risk and how that can be priced. For example, which party bears the risk of inflation or changes in law is determined through the use of options, as are the requirements for parent companies guarantees, performance bonds or advance payment to contractors. The optional clauses are not however limited to these traditional commercial points but also allow a wider consideration of the commercial bargain by including for early completion bonus, the use of key performance indicators and incentives as well as allowing for whole life costing and early contractor involvement.

For parties who are looking for a higher degree of collaboration, that is also provided for. Option X12 provides for multi-party collaboration, which allows the inclusion of other parties such as

designers and strategic subcontractors as part of the overall management of the project. Early Contractor Involvement, under option X22, is another way for the client and contractor to collaborate on the basis of using two distinct stages which allow for a better developed plan for the project with more certainty of the outcome. More recently, the publication of the NEC Alliancing Contract provides a standard form of contract that gives rise to a 'pure' alliance' which includes an alliance board that is responsible for delivery as well as a prohibition on claims between the parties.

## **Dispute Resolution**

As noted above, the costs of resolving complex and substantial construction disputes can have a serious impact on the financial success of a project, as well as diverting resources from more productive activities and damaging long term relationships. The risk of such disputes can be reduced through collaboration but NEC recognises that differences can arise during projects which need to be resolved efficiently in order to avoid harmful escalation. While NEC provides for a tribunal to be used for dispute resolution in the traditional way, it also provides two other alternatives that will help avoid referrals to the tribunal.

The first is the provision for a dispute to be referred to senior representatives. This reflects what often will happen in practice and by embedding that process within the contract, this encourages this option and provides a clear procedure that the parties can follow. The second is the option to use Dispute Avoidance Boards which are made of one or three members who visit the site regularly and assist the parties to resolve potential disputes before they escalate. Where that is not possible, the Dispute Avoidance Board provides recommendation for resolving it. Again, there is an increasing use of such boards to resolve disputes on international projects and the inclusion of such an option highlights this as something the parties may wish to consider and which has real potential to help projects reach a successful outcome.

## **Conclusions**

International infrastructure projects will inevitably involve parties from different countries and a strong desire to manage costs efficiently and avoid a costly and time consuming dispute after the works are complete. The NEC forms of contract, which use concise drafting and plain English, together with an emphasis on collaboration and contemporaneous assessment, is a modern form of contract that is designed to help international projects achieve a successful outcome.