



Welcome to the August 2015 edition of *Insight*, Fenwick Elliott's newsletter which provides practical information on topical issues affecting the building, engineering and energy sectors.

This issue examines compensation events. In particular, what might constitute a compensation event under NEC3, the possible approach of the English court in relation to the time bar provision at clause 61.3. The practical points arising in relation to both these issues are also considered.

What is a compensation event?

Compensation events are events which are usually not the fault of the contractor and change the cost of the work, or the time needed to complete it. As a result, the prices, key dates or the completion date may be reassessed, and in many cases the contractor will be entitled to more time or money.

Examples of compensation events

NEC3 does not provide a definition of what might constitute a compensation event, but there is a list of specific compensation events at clause 60.1. The list includes:

- actions by the employer (i.e. an employer's failure to allow a contractor access to and use of the site by the agreed date);
- actions by the project manager (i.e. when the project manager gives an instruction to stop or not start any work);
- actions by the supervisor (i.e. when the supervisor instructs the contractor to search for a defect and no defect is found);
- actions by others (i.e. other contractors or statutory bodies affecting the project); and
- other events which are outside the control of either party (i.e. extraordinary weather conditions that would occur less than once every ten years).

Whilst the list is fairly extensive, it is not exhaustive in that there are additional compensation events elsewhere in the NEC3 form, such as those that arise from an employer breach and employer risk events. The former is particularly important as it covers any failure by the employer to comply with its contractual obligations.

Practice points

(1) To ensure you take full advantage of all the compensation events that are available to you, familiarise yourself with:

- the list of employer risks at clause 80.1;
- any additional risks which may appear in part 1 or part 2 of the contract data;
- any Z clauses;
- any main option clauses; and
- any secondary option clauses that might apply².

(2) If the employer breaches any express or implied terms of the contract, don't forget to notify as any breach by the employer will trigger a compensation event under clause 60.1(18).

Notification of compensation events

The aim of the compensation event regime is for compensation events to be assessed as early as possible at the time they incur and not at the end of the project. For this reason, the NEC3 form imposes strict notification provisions. The mechanism for notification depends upon the type of compensation event and there are separate requirements for compensation events arising out of actions by the project manager or supervisor, and compensation events as a result of the contractor becoming aware of an event which he believes to be a compensation event but which has not been notified to him as such by the project manager.

Most importantly, the notification of compensation events may be subject to a time bar at clause 61.3.

Insight

Compensation events under NEC3

This is the second of a three-part series on NEC3.

The first part looked at recent case law on NEC3¹, and this second part looks at one of the most contentious areas of the NEC3 form: compensation events. In particular, we review what might constitute a compensation event under NEC3, and the possible approach of the English court in relation to the time bar provision at clause 61.3 regarding notification of compensation events. The practical points arising in relation to both these issues are also considered.

Part three of the series will come at the end of the year and examine time under NEC3.



Insight

The clause 61.3 time bar

Clause 61.3 provides that if the contractor does not notify a compensation event within eight weeks of becoming aware of the event, he is not entitled to a change in the prices, the completion date or a key date. Depending on the facts and surrounding circumstances, any failure by the contractor to notify a compensation event in accordance with clause 61.3 may operate as a time bar.

There is no direct authority on the clause 61.3 time bar in the context of the NEC3 form, but time bars have occupied the English, Scottish and Irish courts in recent years, and it is therefore worth considering some of the more recent decisions (which differ in their strictness) as they may cast light on the approach the English courts take to the time bar provision under the NEC3 form at such time as it comes to be considered.

The strict approach: WW Gear Construction Ltd v McGee Group Ltd and Education 4 Ayrshire Ltd v South Ayrshire Council

In *WW Gear Construction Ltd v McGee Group Ltd* [2010] EWHC 1460 (TCC), WW Gear employed McGee Group to carry out groundworks for the construction of the Westminster Plaza hotel under the JCT Trade Contract Terms (TC/C) 2002 edition with Amendment No 1: 2003, with further bespoke amendments. Clause 4.21 of the contract prescribed the contractual mechanism for claiming loss and expense which was very similar to the mechanism

for notification under the NEC3 form. Following adjudication proceedings, WW Gear sought a declaration as to the true meaning of clause 4.21, in particular whether McGee was required to comply with it such that it operated as a condition precedent to an application for payment.

Mr Justice Akenhead held that the inclusion of the words “provided that” in clause 4.21 was an effective precondition to the recovery of loss and/or expense and it was clear by the drafting that the parties had intended for the clause to operate in this way.

The strictness of the courts’ approach to time bars was considered further in *Education 4 Ayrshire Ltd v South Ayrshire Council* [2009] CSOH 164. This was a Scots law case in which the council engaged the contractor in relation to groundworks for the design and construction of six new schools under a project agreement. Clause 17.1. of the project agreement provided that upon becoming aware of a delay to the target service availability date, the contractor was obliged to give notice to the council, setting out reasons for the delay and its likely effect. The clause further provided a procedure whereby the contractor could claim an extension of time and compensation if the delay constituted a “Works Compensation Event”. The works fell into delay when asbestos was discovered on site and the contractor sought to recover compensation in respect of the delay. The contractor had written to the employer informing the employer of the delay but failed to follow the correct contractual procedure by which an extension of time and compensation should be sought.

Lord Glennie held that the only question before the court was “what did the clause require?” In

circumstances where the parties had laid down in clear terms what had to be done if certain relief was to be claimed, Lord Glennie took the view that the court should be slow to relieve a party that did not comply. The contractor’s claim for an extension of time and compensation was therefore disallowed.

Applying this strict application to the NEC3 form, the wording of clause 61.3 leaves little doubt that a condition precedent is anticipated by the parties, unless the facts and circumstances suggest otherwise (as to which see further below).

A recent relaxation of the strict approach: Obrascon Huarte Lain SA v Her Majesty’s Attorney General for Gibraltar

Following the decision of the Technology Construction Court in *Obrascon Huarte Lain SA v Her Majesty’s Attorney General for Gibraltar* [2014] EWHC 1028 (TCC)³, there may be scope to depart from the strict approach. Here, the claim was for an extension of time and repudiatory breach under the FIDIC Yellow Book which contains a similar provision to NEC3 clause 61.3 in that the Contractor is to give notice to the Engineer, describing the event or circumstance giving rise to the claim as soon as practicable, and not later than 28 days after the Contractor became aware, or should have become aware, of the event or circumstance (sub-clause 20.1).

On the facts, Mr Justice Akenhead held that OHL was in principle entitled to the seven-day extension of time it claimed, but the availability of the claim for an extension of time was subject to OHL first complying with the condition precedent at sub-clause 20.1. As a matter of construction and practical application, the court found



Insight

that the event or circumstance giving rise to the claim for an extension of time must occur first, following which there must be either awareness by the contractor, or else the means of knowledge or awareness of the event or circumstance prior to the condition precedent must become operative. Awareness is therefore not necessarily expected to be prospective, and Mr Justice Akenhead's decision appears to remain good law as it was not considered or otherwise commented upon by the Court of Appeal when it heard OHL's appeal in July 2015.

Applying this decision to the NEC3 form, in the absence of a requirement in relation to timing of the notification, it may be possible to argue that the event giving rise to the notification must occur prior to notification being possible, which would mean that an extension of time may be able to be claimed either from the time when it was clear there would be delay, or from the time when the delay had actually begun, extending considerably the period during which the contractor is able to serve notice.

Whether such an approach might extend to clause 61.3 of the NEC3 form remains to be seen as there is currently no authority regarding from when time might start to run.

Waiver of the time bar: City Inn Ltd v Shepherd Construction Ltd

Occasionally, the employer may be aware of the circumstances behind the contractor's claim for an extension of time and compensation, in which case the employer may be prevented from later arguing that the contract

provisions had not been properly complied with. In *City Inn Ltd v Shepherd Construction Ltd* [2010] ScotCS CSIH 68 (another Scots law case) the contractor's claim for an extension of time was subject to a condition precedent that the contractor was to provide details of the estimated effect of an architect's instruction within ten days under clause 13.8 of the contract. During the employer's detailed discussions with the contractor in relation to the extension of time, the employer did not once cite the contractor's failure to comply with clause 13.8 as the reason for its refusal to grant an extension of time. In the circumstances, the Court of Session took the view that the employer's silence in respect of clause 13.8 clearly demonstrated that it had departed from and abandoned its contractual right to insist that the contractor was to comply with the provisions of clause 13.8.

If circumstances permit, it may also be possible for contractors to run this argument in relation to the NEC3 form.

A possible exception to the time bar — NEC3 PSC: Northern Ireland Housing Executive v Healthy Buildings (Ireland) Limited

It is worth mentioning that there may be one important exception to the time bar rule under clause 61.3 of the NEC3 Professional Services Contract ("NEC3 PSC") following the decision of the Northern Ireland Court of Appeal in *Northern Ireland Housing Executive v Healthy Buildings (Ireland) Limited* [2014] NICA 27.

Healthy Buildings was engaged by the Housing Executive under a NEC3 PSC to provide asbestos management services at housing association properties. The scope of services to be provided was the carrying out of asbestos surveys, sampling and analysis in accordance

with Health and Safety Executive (HSE) guidance which allowed Healthy Buildings to presume that asbestos was present in certain circumstances, thereby avoiding the need to carry out asbestos sampling in every case.

The time bar under the NEC3 PSC provides:

"If the Consultant does not notify a compensation event within eight weeks of becoming aware of the event, he is not entitled to a change in Prices, the Completion Date or a Key Date unless the Employer should have notified the event to the Consultant but did not" (emphasis added).

At a meeting on 10 January 2013, the Housing Executive made it clear that Healthy Buildings was required to carry out significantly more sampling work than was required by the HSE guidance. A dispute then arose as to whether (i) the instruction given at the meeting in January 2013 constituted a change to the Scope (and therefore a compensation event), and whether (ii) Healthy Buildings' claim for a compensation event failed because notification was given more than eight weeks after the instruction.

Lord Justice Girvan, delivering the leading judgment, found that by imposing a more onerous sampling obligation on Healthy Buildings, the Housing Executive had changed the Scope which was a compensation event pursuant to clause 60.1(1) of the NEC3 PSC. The court found that the eight-week time bar did not apply as the employer should have given notice of the instruction at the January meeting but did not.



Insight

Practice points

- In the absence of English judicial certainty regarding clause 61.3, it is best to adopt a very cautious approach. If you think an event may be a compensation event, notify it as soon as possible. This will prevent arguments and possible disputes as to notification and the timing of any notification later on.
- If you notify late, you may be able to argue that time starts to run for the purposes of clause 61.3 from the time when the delaying event actually started causing delay which may extend the notification period and bring you within it.
- If you fail to notify, or notify late, and the employer fails to take the point that clause 61.3 operates as a time bar, it may be possible for you to argue that the employer has waived its entitlement to rely on the strict provisions of the notification clause. The same reasoning applies if the notification was defective in any way and the employer similarly fails to object.
- Under the NEC3 PSC, you may be able to argue that the time bar does not apply if the employer should have notified the consultant about the compensation event but did not.



Conclusion

The key to success as regards compensation events and the notification of compensation events is familiarity with the contract provisions and good contract management, but in order for the contractor to reap the full benefits, compensation events need to be first identified and then properly notified.

Footnotes

1. See <http://www.fenwickelliott.com/research-insight/newsletters/insight/47>.
2. Main option clauses B and D explicitly permit additional compensation events, and option X2, clause X15.2 and option Y(UK) 2, clause Y2.4 contain further compensation events relating to (i) changes in the law of the country in which the site is located; (ii) the contractor correcting a defect for which he is not liable; and (iii) the contractor exercising his right under the Housing Grants, Construction and Regeneration Act 1996 to suspend performance.
3. See further <http://www.fenwickelliott.com/research-insight/newsletters/insight/43>.

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