December 2023

CECA NEC4 Bulletin

CECA Member Briefing:

Bulletin No. 36 - Payments

Introduction

Training and development support is a key part of CECA's core offer for its membership and working in conjunction with GMH Planning it has delivered a programme of training events around the NEC Form of Contract across several CECA UK regions.

In addition to this training, a series of monthly NEC Contract Bulletins are being produced for both Contractors and Subcontractors to improve practical awareness on key topics within the NEC. The coverage, whilst not exhaustive, is intended as a general overview on some of the contractual principles to increase a wider understanding in support of more sustainable outcomes.

For the purposes of these bulletins a contractual relationship between a "Client" and "Contractor" is assumed. The same rules/principles also apply if the contractual relationship is between a "Contractor" and a "Subcontractor" and so the term "Contractor" will be used to describe both parties.

These bulletins are based on the latest NEC4 family of contracts, but the same principles and rules would apply where parties are engaged under an NEC3 form of contract.

Coming next month:

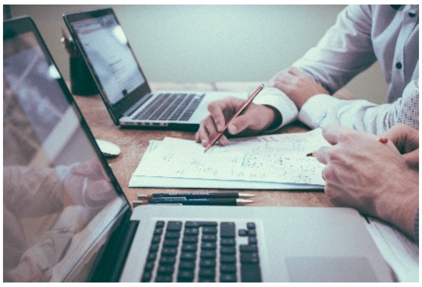
Bulletin Nr 37 - Top ten most important NEC4 ECC/ECS clauses

Please respond to Leone Donnelly should you require any further information on the CECA NEC4 Bulletins via e-mail: leonedonnelly@cecasouth.co.uk.

For further advice or guidance on the NEC details please visit www.gmhplanning.co.uk or contact GMH Planning Ltd by e-mail glenn@gmhplanning.co.uk.

NEC Contract focus month 36 - Payments

Section 5 is the main section of the contract that deals with payments and general commercial matters. Contractors need to make a sustainable margin on any project to be able to reinvest in the future of their own organisation. They invest a considerable amount of resource and cost before even getting into Contract and generally only receive payment when delivering under the Contract. They also need to proactively cashflow throughout as it is not generally their function to fund the project. This bulletin will consider these matters to help a Contractor to achieve those objectives.



Assessing the amount due: The Project Manager will determine each period the amount the Contractor will be paid. The frequency of the payment applications will be identified in contract data part 1 (typically either every four weeks or per calendar month. The Contractor submits an application before each assessment date, including sufficient detail of how it has been assessed. The amount due will be the "Price for Work Done to Date", plus/less other amounts to be paid or retained from the Contractor. Examples of "other amounts" would be retention if X16 included, delay damages if X7 included (and Contractor is running late), and Client cost incurred for a Contractor failing to meet a Key Date (see clause 25.3). It is now a clear obligation under NEC4 for a Contractor to submit an application by the due date, otherwise it could be assessed as zero that period by the Project Manager (see clause 50.4). There is also the potential for 25% of the due amount to be withheld if the Contractor has not submitted the first programme for acceptance which shows the information the contract requires (and one is not already identified in contract data 2).

The rules assessing the Price for Work Done to Date vary between the options:

- option A – completed activities on the Activity Schedule
- option B – quantity of work completed for each item in the Bill of Quantities multiplied by the rate, and the proportion of each lump sum that has been completed
- option C/D/E – total Defined Cost (the cost of the components in the Schedule of Cost Components less any Disallowed Cost) forecasted to be paid by the Contractor* before the next assessment date plus the Fee
- option F – total Defined Cost (amounts paid to Subcontractors and prices for work done by Contractor) forecasted to be paid by the Contractor* before the next assessment date plus the Fee

* for options C/D/E/F the application includes all the costs incurred to date but also a forecast for the next period's costs within that application. The logic behind this is that by the time the Contractor gets paid it will cover the cost incurred, and any errors on the forecast will simply be addressed as part of the "actual cost" assessment the subsequent period.

Payments: The Project Manager certifies a payment within one week of each assessment date. They should also state details of how it has been assessed, particularly if it is lower than the Contractor applied for. The first payment is the amount due, and subsequent payments are the change to the amount due since the previous assessment. This means that applications will be cumulative and the Contractor is paid the difference each month compared to the previous month. If a Contractor has applied for £100k each month for the first six months, the seventh application will be £700k. They will be paid the full amount in the cumulative application, less what has already been paid i.e. less £600k and will receive that month £100k. This makes it easier for the Project Manager to correct any errors in previous assessments as the amount being applied for will always be the cumulative amount. A payment is made by the Contractor if the assessment is ever lower than has already been paid, otherwise payments are made by the Client to the Contractor each period. Each certified payment is made within three weeks of the assessment date unless a different period is stated in Contract Data. Interest is payable on any late payments or later corrected amounts.

Defined Cost: Any Contractor's costs which are not included in the Defined Cost are treated as being included within the Contractor's Fee. NEC4 has simplified compared to NEC3 where there were multiple fee percentages (e.g. subcontract fee, direct fee, working area overhead, people overhead) and there is now a single fee percentage. Any such Defined Cost will be based upon rates and percentages stated in contract data, and any other amounts at open market or competitively tendered prices (and include deductions for discounts or rebates that the Contractor can recover).

Final Assessment: NEC4 now includes a new section (53) for final assessment. This just formalises and allows a more structured finish to the contract tying up all the final payment amounts. The Project Manager makes a final assessment of the amount due no later than four weeks after the Supervisor issues the Defect Certificate, or thirteen weeks after the Project Manager issues a termination certificate. It also allows the Contractor to issue the Client an assessment of the final amount due if the Project Manager does not make this assessment within the time permitted. The Client makes the final payment within three weeks of this assessment, and it would be treated as being accepted if no response has been received within those three weeks (unless the Client referred the matter for dispute under W1/W2/W3).

Schedule of Cost Components: This element has already been covered in a previous bulletin which would be useful to read in parallel to this one (bulletin 23: Defined Cost and Schedule of Cost Components) but in summary:

- Short Schedule of Cost Components used for options A/B to assess compensation events (unless it is mutually agreed to use activity schedule or bill of quantity rates on a case-by-case basis)
- Schedule of Cost Components used for options C/D/E/F to assess compensation events, but also to assess the basis of an application each period
- each of the eight headings within the two schedules detail what the Contractor is able to claim for, and any other costs that do not fit in any of the categories should have been allowed for within the Contractor's fee percentage

Tendered total of the Prices: For options A/B/C/D the Contractor will confirm their tender price as the "total of the Prices" as an entry in contract data part 2. This will align with the total amount on their activity schedule (for options A&C) and the bill of quantities (for options B&D) submitted as part of their tender submission. For option E, there is no tender price submitted and only a fee percentage offered, which will be applied to the Defined Cost incurred. For option F which is the rarely used "Management Contract", the only Prices the Contractor offers at tender stage is any work that they will do themselves as opposed to everything else which is subcontracted and managed by the Contractor, for which they will be entitled to their fee percentage on top of incurred Subcontractor costs.

Disallowed Costs: For options C/D/E/F the Contractor has to be very wary of not doing anything that could constitute a "disallowed cost" that would not be paid. This is particularly important for options E&F, where these could very quickly eat into the amount of recoverable fee percentage which is the only cost the Contractor is able to recover under these options. This subject matter is covered in more detail within bulletin 31 (Disallowed Costs).

Records: For options C/D/E/F there is a clear obligation to keep records to assess the validity of the Defined Cost claimed by the Contractor. The Project Manager has the right to inspect these records at any time (within working hours). These records include amounts of payments of Defined Cost, proof that payments have been made, communications and assessments of Subcontractor's compensation events, and any other records as stated in the Scope. This means these options are fully "open book" as the Contractor will need to demonstrate they have been properly incurred (otherwise could be a "disallowed cost"). This requirement to be able to demonstrate Defined Cost will also therefore mean more management resource to produce and scrutinise accordingly for both Parties.

Summary: Getting the correct tender price and fee percentage to start with and maintaining a good cash flow during the life of a project is absolutely fundamental to a Contractor's success. The rules of the contract in this regard therefore need to be understood and followed to minimise any negative impact this could otherwise have.