



ADJUDICATION UNDER THE NEC3

Jeremy Glover

6 October 2007

ARBRIX

Introduction

1. I often think of the NEC3 as the marmite contract you either “love it or hate it”.¹ In debate, there often appears to be little middle ground. However, whatever your view, it is clear that the NEC3 is a contract which is often used, and which is likely to be used more frequently both at home and abroad.
2. The basic philosophy behind the NEC3 can be found in the opening paragraph of the Procurement and Contract Strategies document, which states that the:

NEC is a modern day family of contracts that facilitates the implementation of sound project management principles and practices as well as defining legal relationships. Key to the successful use of NEC is users adopting the desired cultural transition. The main aspect of this transition is moving away from a reactive and hindsight based decision making and management approach to one that is foresight based encouraging a creative environment with proactive and collaborative relationships.

3. The purpose of this paper is threefold:
 - (i) to review the adjudication provisions to be found in the NEC3;
 - (ii) to consider the application of these provisions to London 2012; and, finally,
 - (iii) to discuss one or two of the more fertile areas for dispute and hence those areas which are likely to feature in any adjudication commenced under the NEC3 contract.

Adjudication under the NEC3

4. The NEC3 was published in July 2005. Whilst it retained many of the same basic features as its predecessor, the dispute resolution provisions, Options W1 and W2, are new. The NEC3, do not forget, is marketed as an international contract. One adjudication option covers the UK; the other is aimed at the international market.

¹ Slogan, presumably the copyright of Unilever.

5. The principal dispute resolution procedure in NEC3 remains adjudication. One option applies if the Housing Grants Construction Regeneration Act 1996 (“HGCRA”) applies, the other is there for when the HGCRA does not apply.
6. This represents a change from the NEC2. The adjudication procedure in NEC2 included the concept of the “matter of dissatisfaction” and imposed minimum time periods that a referring party had to comply with before they could issue a referral to adjudication. Section 108(3) of the HGCRA requires a construction contract to provide that either party could “at any time” refer a dispute to adjudication. NEC2 therefore fettered the ability of either party to refer a dispute at any time and so did not comply with the HGCRA. As a result, as acknowledged before the courts,² either party could ignore the adjudication provisions in NEC2 and refer any dispute at any time under the HGCRA and in accordance with the adjudication procedure set out in the Scheme for Construction Contracts³ rather than the adjudication procedures set out in the NEC2.
7. NEC3 has dealt with this problem by providing the dispute resolution clauses as separate options. They no longer form part of core clause 9 which has consequently been renamed simply “Termination”. Under the NEC3 there is an HGCRA-compliant procedure at Option W2, while the original clause 90 from the NEC2 adjudication procedure, effectively reappears at option W1.

Features common to both options W1 and W2

8. The NEC3 envisages that an adjudicator will be named under the contract. If that is not done, or the adjudicator resigns or otherwise declines to act, the parties can either agree on the identity of a new one or either party may ask an adjudicator nominating body to appoint one.⁴ Thus the responding party, if it is quick, might be able to have a high degree of influence over any appointment.
9. The adjudicator must act impartially and decide⁵ the dispute. In so doing the adjudicator must act as an “independent adjudicator”, and not as an arbitrator. He should also enter into the NEC3 adjudicator’s contract which can be found in the NEC3 box.
10. If the matter disputed by the contractor under or in connection with a subcontract is also a matter disputed under or in connection with the main contract, provided the parties consent, the dispute between the contractor and subcontractor may be referred to the same adjudicator at the same time.
11. Sub-clauses W1.3(9) and W2.3(9) stress that unless and until the adjudicator has notified the parties of his decision, everyone must proceed as if the matter disputed were not disputed.
12. By clause W2.4:

² See *McAlpine PPS Pipeline Systems Ltd v Transco Plc* [2004] All ER (D) 145 and *Roscco Civil Engineering Ltd v Dwr Cymru Cyfngedig* [2004] All ER (D) 339 (Jul).

³ The Scheme for Construction Contracts (England and Wales) Regulations 1998 No. 649

⁴ W1.2(3) or W2.2(3)

⁵ There has been a small change in the wording; the adjudicator now decides a dispute, whereas before he settled it. This is in keeping with the temporary finality of the adjudicator’s decision.

(1) *a Party does not refer any dispute under or in connection with this contract to the Tribunal unless it has first been decided by the Adjudicator in accordance with this contract.*

(2) *If, after the Adjudicator notifies his decision the party is dissatisfied, that party may notify the other party of the matter which he disputes and state that he intends to refer it to the tribunal. The dispute may not be referred to the tribunal unless this notification is given within four weeks of the notification of the Adjudicator's decision.*

13. Thus the decision is binding unless or until revised by a "tribunal". More importantly, the decision becomes final and binding unless one of the parties, within four weeks, notifies the other that he is dissatisfied with the dispute and intends to refer it to the tribunal.⁶ This is true of both Options W1 and W2.

Option W1

14. W1 identifies a series of potential areas of dispute and sets out which party may refer a dispute and when it may be referred to an adjudicator.

15. There are four areas of dispute:

- A dispute about an action of the project manager or supervisor.

This may be referred to adjudication by the contractor between two and four weeks after the contractor's notification of the dispute to the employer and project manager. The notification must be made not more than four weeks after the contractor became aware of the action.

- A dispute about the project manager or supervisor not having taken a particular course of action.

This may again be referred to adjudication by the contractor between two and four weeks after the contractor's notification of the dispute to the employer and project manager. The notification must be made not more than four weeks after the contractor became aware of the action.

- A dispute about a quotation for a compensation event which has been treated as having been accepted.

This time, it is the employer who may refer the dispute to an adjudicator. He should do so between two and four weeks after the project manager's notification of the dispute to the employer and the contractor. That notification must be made not more than four weeks after the quotation was treated as accepted.

- Any other matter.

Either party may refer a dispute about any other matter between two and four weeks after the notification of the dispute to the other party and the project manager. In other words this is a fall-back or default procedure that can be used by either party.

⁶ W14(3)

16. Indeed, Option W1 can itself be viewed as a default procedure. Provided the HGCRA does not apply, it automatically applies. This is not the only example of a tension between the two adjudication provisions and the NEC3's domestic and international applications. You do not select an option in the contract data. One potential problem with this approach is that if the contract is used somewhere with its own adjudication-type legislation then it may well be the case that option W1 will not comply with the local legislation. This will mean that, as with NEC2, the dispute resolution procedures may be entirely replaced by a local legislation.
17. One way to deal with this potential problem would be to seek a "middle way". In other words, there would be some onus on the parties to check whether options W1 and W2 are appropriate. If they are not, the employer would have to insert a dispute resolution procedure that did comply with the law of the place where the contract is being carried out.
18. The party referring the dispute to the adjudicator must include "information" with the referral. This is no doubt the supporting documentations and explanation of the matter or matters in dispute. Any further information is to be provided within four weeks of the referral.⁷ The adjudicator is to decide the dispute, with reasons, within four weeks of the end of the period from receipt of the information. The period may be extended by agreement between the parties. The minimum period, therefore, for an adjudication under Option W1 is eight weeks.

Option W2

19. This is the more familiar form and is to be used in the UK when the HGCRA applies. Option W2 complies with the HGCRA and makes clear at its outset that:

"a dispute arising under or in connection with this contract is referred to and decided by the Adjudicator. A Party may refer a dispute to the Adjudicator at any time."
20. The parties have the option of identifying a contract-specific adjudicator in the Contract Data. If you are the named adjudicator under the contract, the party wishing to refer the dispute to adjudication will send you a copy of the notice when it is issued. The named adjudicator, within three days of the receipt of the notice, must then notify the parties either:
 - (i) That he is able to decide the dispute in accordance with the contract; or
 - (ii) That he is unable to decide the dispute and has resigned.
21. If the adjudicator does not so notify within three days, either party may act as if the adjudicator has resigned.
22. Note that the dispute must be referred within seven days. Thus, there may only be a four-day window to appoint a fresh adjudicator if you have a contractually named adjudicator who is unable to act or does not respond to the original notice.
23. When referring the dispute, the referring party in the usual way must provide the adjudicator with *"the information on which he relies, including any supporting documents"*.

⁷ Option W1.3(3).

24. Note that clause W2.3 states this:

“Any further information from a Party to be considered by the Adjudicator is provided within fourteen days of the Referral. This period may be extended if the Adjudicator and the parties agree.”

25. This is different from your usual approach of sequential service and appears to apply to both parties. Note that the period can be extended, if everyone concerned agrees.

The adjudicator’s contract

26. The adjudicator’s contract comes with a set of guidance notes. These assume that the adjudicator will be appointed under the NEC3 adjudicator’s contract. This is the case whether or not the adjudicator is named under the contract or was chosen by a nominating body.⁸

27. At the forefront of the guidance note is the following unsurprising but entirely appropriate comment:

“The requirement for the Adjudicator to act impartially is fundamental to the whole system of adjudication. Any failure by the Adjudicator to so act would be a serious breach of his obligations.”

28. Thus, it is important that any matter which affects the adjudicator in the carrying out of his duties is identified. The guidance notes give the example of a contractor entering into a subcontract with a subcontractor with whom the adjudicator may have some, however small, connection.

29. There will inevitably have been some discussion today about the importance of dates and the time by which documents are received. Item 1.10 of the guidance notes confirms that communications are effective *“only when they have been received”*. Thus the date for making a decision runs from the date of receipt not of posting a referral.⁹

30. Item 3 deals with payment. Although the sub-clause begins by noting that the timescale for adjudication does not lend itself to interim payments or holding on to the decision until payment is made, it does appear to permit the use to advance payments to secure the adjudicator’s fee. In the light of the decision of HHJ Coulson QC in the *Cubitt v Fleetglade* case, in which the judge indicated that an adjudicator was not entitled to hold a lien over his fees prior to publication of his decision, there must be some doubt about the applicability of this clause. In reality, the advance payment more properly holds to situations where an adjudicator is named in the contract and is perhaps better suited to the long-term contract and even Option W1-type projects. Thus, an argument can be made that the advance payment is different from an adjudicator seeking a lien over his fees. Of course, the parties to the contract can overcome this by entering the word “nil” in the appropriate box in the contract data.

⁸ Indeed, as the guidance notes say, the contract may also be used for the appointment of an adjudicator under other contract forms.

⁹ The scheme does provide for communications being effective when posted.

31. The reason given by the NEC Guidance Note for the advance payment is to avoid the “possibility of a strategic delay” by one of the parties. Thus, the provision may also be considered to have more relevance to Option W1. Of course, this is another example of the need to keep in mind at all times the nature of the law of the jurisdiction under which the particular contract operates.
32. Item 1.4 of the adjudicator’s contract specifically identifies those expenses for which an adjudicator may charge. These as you would expect include for printing and copying, faxes and telephone calls, postage, travel costs and charges by others for help in an adjudication.¹⁰
33. If you have an adjudicator on board at the beginning of your project, other questions arise. Do the parties want the adjudicator to familiarise himself with the project by visiting the project or having sight of the contract, even though no disputes have arisen? The NEC form makes no provision for this, unlike others such as the FIDIC forms of contract. Indeed, they do so in considerable detail. Whilst the FIDIC form favours the Dispute Adjudication Board (“DAB”), it recognises that on small projects (and by this FIDIC apparently mean a project with a monthly spend of US\$2 million) one adjudicator would be sufficient. Contrast the detailed requirements of DAB Procedural Rules, which include provision for regular site visits, with what is to be found in the NEC3. A truly international contract might be thought to have considered making further provision for its adjudicators.

NEC3: adjudication and the Olympics

34. As is well known, in April 2006, the Government announced that the NEC3 suite of contracts would be adopted for use in all the Olympic contracts. However, it has not adopted the NEC3 adjudication provisions in their entirety.
35. Before discussing what the Government and ODA have decided upon, it is worth briefly looking at previous Olympic projects.

Sydney 2000

36. For the Sydney Games there was a multi-tiered dispute resolution procedure.
37. For disputes between the Olympic Co-Ordination Authority (“OCA”) and the Special Purpose Vehicle (“SPV”) set up to deliver the main stadium and other venues, a Dispute Resolution Committee (“DRC”) was set up. This committee included representatives from both parties and the aim was that it met within five days of a dispute being referred to it in an attempt to resolve that dispute. The DRC then had 20 days to resolve the dispute, unanimity being required.
38. If this failed, then the heads of the OCA and the SPV would meet to see if they could in good faith resolve the issue. They were given 10 days. If this failed then, within 28 days, either party could refer the dispute to expert determination. This would be binding unless the dispute was for greater than AUS\$5million or a notice of dissatisfaction was given within 14 days.

¹⁰ Provided of course an adjudicator has made clear that he intends to elicit the help of others.

39. The SPV and the Main Contractor agreed to be bound by any decision of the DRC which affected them, otherwise the resolution of disputes would follow a similar form. Of course, parties were expected to continue to progress their works pending the resolution of disputes.
40. For disputes involving the Organising Committee, the dispute resolution procedures were similar but required that the parties use all reasonable endeavours to avoid disputes and there was provision for a mandatory reference to mediation.

Athens 2004

41. I am not entirely sure what happened in Greece, save of course that amidst much initial scepticism, the facilities were duly completed on time.

Beijing 2008

42. Mediation has a long long history in China. There are many traditions. For example, over 4,000 years ago, Shuen was king along the Yellow River. The people living in the mountains quarrelled about the borders of their land, people living beside the lakes argued about the ownership of their houses, and people living along the rivers made and sold pottery of very bad quality. In order to solve these problems, Shuen himself went to each area to farm, to fish, and to make pottery with his people. After one year of his instruction, so the story goes, the mountain dwellers started offering their lands to each other; the lakeside residents started conceding their houses to each other; and those living along the rivers started making and selling pottery of a very good quality.¹¹
43. Under the Ming dynasty every village had to construct a "shenming" pavilion¹² where the local old folk would listen to the disputes of the local people as judges and try and resolve them.
44. For the Olympic projects there is a two-tier dispute resolution system. The first involves negotiation, be it structured or otherwise; if this fails then there are provisions for arbitration. Even under arbitration, there is provision for the arbitrator to act as a conciliator,¹³ something which, of course, UK adjudicators should only consider doing with the greatest care, if at all.¹⁴
45. The dispute resolution system provides for neither dispute boards nor expert determination.

London 2012

46. Although the NEC3 suite is to be used, the adjudication and dispute resolution provisions have not been wholeheartedly adopted.
47. The Procurement Principles for the Games say this:

"the strategy will commit Olympic Procurement disputes to alternative dispute resolution wherever possible."

¹¹ See Pei, Cao "The origins of mediation in traditional China", *The Dispute Resolution Journal*, May 1999 for more details and information

¹² "Shenming" in Chinese means "making reasons clearly"

¹³ Article 40 of the CIETAC rules, the Chinese arbitration rules.

¹⁴ *Glencot Development & Design Co Ltd v Ben Barrett & Son (Contractors) Ltd*

48. Whatever the contract says, this will include the right to adjudicate at any time. As Mr Justice Dyson said, the words of section 108 of the HGCRA mean exactly what they say¹⁵ and as mentioned above the adjudication provisions in the second edition of the NEC form had to be amended as they appeared to fetter the right to adjudicate.
49. Ensuring that disputes can be resolved easily will be a key factor in determining whether the contracts are executed on time and on budget. An adequate dispute resolution procedure needs to be in place in order to deal promptly and fairly with any issues that arise. The ODA are currently in the process of establishing a Dispute Board.
50. The collective term Dispute Board covers both the concept of Dispute Review Boards and Dispute Adjudication Boards. The basic idea is that the board will evaluate disputes during the course of the project and, if it is the American form of Review Board, make a non-binding settlement recommendation to the parties. With a Dispute Adjudication Board, the board considers submissions from the parties and then issues a written binding decision. The parties are obliged to comply with the decision, and unless they issue a notice of dissatisfaction within 28 days of the giving of the decision, the decision becomes final and binding.
51. Over time, the board will gain familiarity with the project and the individuals working on it. This means that if a dispute arises the board members understand the project and have already built some rapport with the individuals working on the project. They can then deal with disputes by hearing presentations from the parties and suggesting solutions.
52. Of course, given the Procurement Principles outlined above, it may well be that the contracts, once let, will include provisions for mediation, (even project mediation), or expert determination. That is a matter for negotiation between the parties.
53. One new alternative can be found in the FIDIC D-B-O¹⁶ contract launched on 13 September 2007. Sub-clause 20.4 states:
- If at any time the Parties so agree, they may jointly refer a matter to the DAB in writing with a request to provide assistance and/or informal discussion and attempt to resolve any disagreement that may have arisen between the Parties during the performance of the Contract. Such informal assistance may take place during any meeting, site visit or otherwise. However, unless the Parties agree otherwise, both Parties must be present at such discussions. The Parties are not bound to act upon any advice given during such informal meetings, and the DAB shall not be bound in any future Dispute Resolution process and decision by any views given during the informal assistance process, whether provided orally or in writing.
- If a dispute of any kind whatsoever arises between the Parties, whether or not any informal discussions have been held under this Sub-clause, either Party may refer the dispute in writing to the DAB according to the provisions of Sub-Clause 20.5 [Obtaining Dispute Adjudication Board's Decision].
54. This clause certainly has a collaborative feel to it and may have been inserted as an acknowledgement of the long-term, 20-year nature of the D-B-O arrangement.

¹⁵ *Herschel v Breen Engineering*

¹⁶ Design-Build-Operate

Disputes under the NEC3

55. Perhaps, especially with 2012 in mind, perhaps this section should really be headed “avoiding disputes”, and the key to that is knowing and understanding your contract and the contractual relationships you have entered into.
56. A key reason why the NEC3 contract has been chosen is because of its partnering-based approach to the resolution of issues and disputes. The basic idea is that co-operation by the parties from an early stage of any issue identified by the contractor or project manager will provide the opportunity for the parties to discuss and resolve the matter in the most efficient manner, perhaps before the need for adjudication arises.
57. The scope for discussing the potential for disputes under the NEC3 is of course, as under any construction contract, vast. What I have done is to choose a few of the key and better known features of the NEC3 and I intend briefly to discuss the extent to which they well crop up in any dispute.

Flexibility

58. One of the core features of the NEC3 is flexibility. It is said that the NEC3, with its menu of main and secondary Options, can be used for any procurement method in an international, multi-discipline environment (be it building, civil, process engineering) and whether it includes contractual design or not. At the heart of the NEC3 contracts are the nine core clauses. From these, a user selects the appropriate main option clause then considers the 15 secondary option clauses and finally can consider whether or not to insert certain bespoke terms or amendments from the Z clauses. In addition to this, there are two different schedules of cost components.
59. The immediate downside here, for those who are not experienced in dealing with the NEC form or for those who do not take sufficient care when compiling the contract, is that ultimately there may not actually be a contract or, in terms of adjudication, there may not be a contract sufficiently evidenced in writing to enable an adjudication to take place. The consequences of the *RJT*¹⁷ case are well known and it remains to be seen whether, and if so when, the Government will introduce its reforms to the HGCRA which, as things stand, will overrule the *RJT* decision.
60. To take one decision, in *Mast Electrical Services v Kendall Cross Holdings Limited*,¹⁸ disputes arose between the parties over what rates, if any, had been agreed. Although specific quotations had been submitted, Mr Justice Jackson was of the view that the documents relied upon by Mast did not set out or record all the agreed rates of payments. Thus, it was highly probable that there was no contract at all, let alone one evidenced in writing.
61. Under current provisions of the HGCRA, this is a potential ground for disagreement in relation to adjudication when the NEC3 form is used.

¹⁷ [2002] EWCA Civ 270

¹⁸ [2007] EWHC 1296 (TCC)

62. Two of the aims of the original NEC Drafting Committee¹⁹ were to achieve a high degree of clarity when compared with other existing contracts and to use simple, commonly occurring language and avoid legal jargon. Certainly the latter of these two aims has been achieved. However, question marks have been raised as to whether it is at the expense of the first aim, namely clarity.

63. To take the example of contractor design: core clause 2 deals with the contractor's main responsibilities. Under clause 21.1:

The contractor designs the parts of the works which the works information states he is to design.

64. Under clause 21.2:

The contractor submits the particulars of his design that works information requires to the project manager for acceptance

65. Under clause 21.3:

The contractor may submit his design for acceptance in part if the design of each part can be assessed fully

66. Core Clause 27.1 states that:

The contractor obtains approval of his design from others where necessary.

67. It is not entirely clear from this clause alone to whom the contractor has to submit drawings for approval, what the criteria for establishing approval is and what happens if that approval is not provided.

68. This can be contrasted with clause 4.1 of the FIDIC Red Book.²⁰ Clause 4.1 deals with the contractor's general obligations. Where the contract specifies that the contractor shall design any part of the works then sub-clause 4.1 makes it clear that:

(a) the Contractor shall submit to the Engineer the Contractor's documents for this part in accordance with the procedure specified in the Contract;

(b) These Contractor's documents shall be in accordance with the Specification and Drawings, shall be written in the language for communications defined in sub-clause 1.4 [Law and Languages], and shall include additional information required by the Engineer to add to the Drawings for co-ordination of each Party's design;

(c) The Contractor shall be responsible for this part and it shall, when the works are completed, be fit for such purposes for which the part is intended as are specified in the Contract; and

(d) Prior to the commencement of the Tests on Completion, the Contractor shall submit to the Engineer the "as billed" documents and operation and maintenance manuals in accordance

¹⁹ Principally led by Dr Martin Barnes

²⁰ The Conditions of Contract for Construction for Building and Engineering Works Designed by the Employer: The Construction Contract.

with the Specification and insufficient detail for the employer to operate, maintain, dismantle, re-assemble, adjust and repair this part of the works.

69. The extent of the contractor's obligations is made perfectly clear. Whilst the extent of the contractor's obligations under the NEC3 form are potentially also made equally clear,²¹ it might have been considered more helpful if they had been made clear in one specific place.
70. I accept of course that the NEC3 starts from the notion that there is a single form of main contract and that flexibility is obtained by selecting one of the main pricing options, and then, as appropriate, from a list of secondary clauses. Experience suggests not everyone will get it right.

Partnering

71. I suspect it may be an unwritten rule that any paper written by a lawyer about the NEC3 must mention clause core clause 10.1. Far be it from me to deviate from this principle. Core clause 10.1, of course, states:

"The Employer, the Contractor, the Project Manager and the Supervisor shall act as stated in this contract and in the spirit of mutual trust and co-operation."

72. I am not the first to note that whilst the NEC3 form has made a point of avoiding the use of the word "shall" it appears in core clause 10.1. The simple problem is, what does this clause mean?
73. Now, there are an increasing number of construction contracts which impose a duty of good faith. For example, the concept of good faith does sit quite easily with a number of the new arrangements in procurement, such as partnering or alliance relationships or for longer-term relationships based on undertakings to act in good faith. With these long-supply contracts, distribution systems based on franchises, employment relations and term contracts there is a need to evolve mechanisms for recognising and supporting expectations for flexibility, co-operation and to support the development of these long-term relationships. This is one reason for the introduction of the new FIDIC clause, sub-clause 20.4, discussed above.
74. Core clause 10.1 comes close to a requirement to act in good faith. That said, it should be noted that the first part of sub-clause 10.1 requires the parties to act in accordance with the provisions of the contract. Thus, the core clause reflects the good faith requirements of those countries that operate under a civil code. For example, article 148 of the Egyptian civil code states that:

"a contract must be performed in accordance with its contents and in compliance with the requirements of good faith."

²¹ Option X-15 applies. If the *contractor* is designing as well as installing the *Works* then unless Option X15 is selected it is possible that the design will have to be fit for purpose (see *Independent Broadcasting Authority v EMI Electronics* (1980) 14 BLR1).

75. As a consequence, the requirement for the parties to act in a partnering context, does little to change their respective responsibilities under the contract as a whole. I think it noteworthy that the NEC3 makes no attempt to define what it means by “mutual trust and cooperation”.²²
76. For example, in the case of *Bedfordshire County Council v Fitzpatrick Contractors Limited*,²³ Dyson J would not imply such a term into a road maintenance contract that neither party should conduct itself in such a way that would “*damage the relationship or confidence in trust*” between them. One reason for this was the care taken by the parties to detail out the terms which were to govern their contract. There was no scope to imply this further relationship.
77. Of course, there is a difference between implying a term and enforcing a term upon which the parties have agreed. Therefore, it is likely that the courts will need to consider the term, even though they may well be met with doubts that the clause is too uncertain to be enforceable. Whether or not it becomes a clause the courts will be asked to consider, there is no doubt that it is a clause the parties will refer to in any dispute before an adjudicator.
78. Although good faith will not be implied by the courts, it is being found (and considered by the courts) in an increasing number of contracts. For example, in the case of *Petromec Inc and Others v Petrobras and Others*,²⁴ the Court of Appeal had to consider the following contractual term:
- B agreed to negotiate in good faith with P the extra cost referred to in [the Contract].*
79. The term was drafted by solicitors and expressly agreed by the parties. LJ Mance said:
- The traditional objections to enforcing an obligation to negotiate in good faith are (1) that the obligation is an agreement to agree and thus too uncertain to enforce, (2) that it is difficult, but not impossible, to say whether, if negotiations are brought to an end, the termination is brought about in good or in bad faith, and (3) that, since it can never be known if good faith negotiations would have produced an agreement at all or what the terms of any agreement would have been if it would have been reached, it is impossible to assess any loss caused by breach of the obligation. I doubt, however, if any of these objectives would be good reasons for saying that the obligation in negotiating good faith contained in clause 12.4 is unenforceable in this particular case.*
80. There were two reasons for this. First the requirement was expressly agreed by the parties as part of a contract drawn up by lawyers. Second, the Court recognised that it would be able to calculate the cost referred to and so would be able to establish whether there was a lack of good faith on the part of anyone.
81. In considering the position, adjudicators should recollect that it does appear that the English courts will pay attention to the intentions of the parties. Thus, as is well known, in *Birse Construction v St David Limited*²⁵ HHJ LLOYD QC held that the terms of a partnering charter

²² In fact, the explanatory guidance notes merely state that the requirement was added on the recommendation of the 1994 Latham report entitled *Constructing the Team*.

²³ (1998) CILL1440

²⁴ [2005] EWCA Civ 891

²⁵ [1999] BLR 194,

which was not and was never intended to be a binding contract, even though it had been signed by the parties:

clearly not legally binding, are important for they were clearly intended to provide the standard by which the parties were to conduct themselves and against which their conduct and attitude were to be measured.

82. The Judge accordingly considered that the conduct of the parties and the context of the partnering charter in deciding when and whether a contract had been concluded.²⁶ This is the approach that any judge or adjudicator should follow if asked to consider the effect of core clause 10.12.
83. It is likely that the first such challenges will be in the sphere of procurement. In June, the case of *Gerald Martin Scott & Others v Belfast Education & Library Board* was heard in the High Court of Justice in Northern Ireland, Chancery Division.
84. Gerald Martin Scott ("Scott") were tendering contractors for a contract to be placed by the Belfast Education and Library Board ("the Belfast Board"). It appears that Scott sought an interim injunction restraining the Belfast Board from proceeding with a tendering process due to mistakes and/or ambiguities in the tender documents which, Scott argued, meant that the tenderers could not tender on an equal basis.
85. Scott argued that there was an implied contract between tenderers and prospective employers and that an implied term of that contract was one of fairness and good faith. The Belfast Board rejected this argument.
86. However, the court agreed that the tender documents did give rise to an implied contract, the terms of which are that the employer must act fairly and in good faith. One of the terms to be implied was that there should not be any material ambiguity in the tender documents that would significantly affect the tender.
87. Mr Justice Weatherup said this:

[6] Having considered all of the authorities and without reviewing them for the purposes of this present ruling I would state as follows. First of all, I am satisfied that an implied contract can arise from the submission of a tender. It may arise by inference from the scheme of the tendering process and the presumed intention of the parties. Secondly, I am satisfied that an implied contract may arise from a tendering process for a public works contract, even though the particular contract is below the financial level of the Regulations that apply in relation to public works contracts. The parties to such a public works contract as the present are parties to an elaborate tendering process which is designed to achieve best value for the provision of public services. An implied contract arises in the present case. Thirdly, I am satisfied that the implied terms of such an implied contract extend to the implied term of fairness and good faith.

[7] The proposed implied term is that of fairness and good faith. Good faith is not an issue in this case. It is a question of fairness. I am satisfied that the concept of fairness applies in a number of respects:

1. Fairness applies to the nature and application of the specified procedures in a particular contract.

²⁶ The first instance decision was overturned on appeal, although the Court of Appeal did not deal with the comments made by the Judge on the charter itself.

2. Fairness applies to the assessment of the tenders according to the stated criteria.

3. Fairness applies to the evaluation of the tenders in a uniform manner and as intended by the tender documents.

88. He considered that if there was a mistake in a tender submitted by a tenderer it may arise by reason of misinterpretation of the documents by the tenderer. If that mistake was occasioned by the employer, for example, because there was an error or ambiguity in the tender documents, then that may give rise to a position where one or more tenderers adopted a different approach to the tender to that which must have been intended by the tender documents. This in turn may affect the assessment of the tenders and may affect the fairness of the process.

89. The Judge also had drawn to his attention a decision of the European Court of Justice in *SIAC Construction Ltd v Mayo County Council*²⁷, which concerned a tendering process for public works by Mayo County Council. A Council Directive on awarding public contract works require Member States to have regard to the procedures provided by the Directive. The decision contained certain observations which relate to such a tendering process, although as the Judge stressed, the Scott case was not governed by the Directive. The Judge noted that

What emerges from the conclusion is

1. The duty to observe the principle of equal treatment of tenderers lies at the heart of the Directive and tenderers must be in a position of equality, both when they formulate their tenders and when those tenders are being assessed by the adjudicating authority.

2. The principle of equal treatment implies an obligation of transparency in order to enable compliance to be verified. Transparency means that the award criteria must be formulated in the contract documents or the contract notice in such a way as to allow all reasonably well-informed and normally diligent tenderers to interpret them in the same way. Further, transparency also means that the adjudicating authority must interpret the award criteria in the same way throughout the entire process.

3. Further, when tenders are being assessed the award criteria must be applied objectively and uniformly to all tenderers. If the documents are not capable of being interpreted by the tenderers in the same way then the process may lose that objective and uniform approach to the assessment of tenders.

90. This is clearly an important case, confirming as it does the proposition that a contract can be implied between a prospective employer and tenderer and further that a term of that implied contract is that the employer will act fairly and in good faith. In this case, a breach of good faith was not argued and the Judge concentrated on what this implied term means in the context of fairness. The Judge made clear that acting fairly extends to a prospective employer ensuring that there are no mistakes or undetected ambiguities in the tender documents which might lead to tenderers tendering on an unequal basis. Potentially, this case could be the springboard for further litigation in this area of procurement.

²⁷ [2002 All ER (EC) 272

91. Indeed, potentially this case could be the springboard for further litigation beyond the area of procurement. Many of the first Antipodean cases²⁸ evolved from the procurement arena.

Early warning and Compensation Events

92. The NEC3 contains express provisions requiring the contractor and project manager to notify an early warning and, if required, call a risk reduction meeting when either becomes aware of any matter which could affect price, time or quality. The NEC3 procedure requires the contractor to price the time and costs defect of a change within 21 days and for the project manager to respond within 14 days. There is therefore what is termed a rolling final account with early settlement and no later end of job claims for delay/disruption. Obviously, if this works, this may turn out to be beneficial for the contractor in terms of cash flow.

93. It is important to note that core clause 63.4 states:

The rights of the Employer and the Contractor to changes to the Prices, the Completion Date and the Key Dates are their only rights in respect of a compensation event.

What are compensation events?

94. NEC3 contracts do not refer to "variations" or "loss and expense". Instead, there are "compensation events". The NEC3 Guidance Notes define these thus:

Compensation events are events which may lead to the payment to the Contract being changed or the Completion Date being delayed.

95. Compensation events are set out in core clause 60.1. They include:²⁹
- (i) Where the project manager gives an instruction changing the Works Information (i.e. a variation).
 - (ii) Where the employer does not allow access to the Site on the dates shown in the Accepted Programme.
 - (iii) Where the employer does not provide information by the dates required in the Accepted Programme.
 - (iv) Where the employer or others (i.e. third parties) do not carry out works in accordance with the Accepted Programme, Works Information, etc.
 - (v) Where the project manager or supervisor does not reply to the contractor within the time limits set down by the contract.
 - (vi) Where the project manager refuses to accept a quotation for reasons not stated in the contract.

²⁸ Although the first, the case of *Renard Constructions (ME) PTY Ltd v Minister for Public Works* (1992) 26 NSW LR 234 involved questions of termination.

²⁹ They include within the unamended core clauses of the NEC 3 over 19 different compensation events. This is just a summary. The list of compensation events is often amended.

(vii) Where the contractor encounters physical conditions on Site which an experienced contractor would have regarded at the Contract Date had such a small chance of occurring it would have been unreasonable for the contractor to have allowed for that event and when judging the physical conditions for assessing a compensation event the contractor is assumed to have:

- considered the Site Information
- considered publicly available information referred to in the Site Information;
- carried out a visual inspection of the Site;
- considered other information which an experienced contractor could reasonably be expected to have or obtained;
- where the weather measurement (which is included in the Contract Data) within a calendar month were compared with the Contract Data occurs on average less frequently than one in ten years.

96. Under the NEC3, where the project manager or the supervisor's actions give rise to a compensation event, it is for the project manager to notify the contractor of the compensation event at the time of giving the instruction. The contractor will at the same time as being given a notice be instructed to submit a quotation but in the meantime he still has to comply with the instruction or changed decision.

97. However, for other matters giving rise to a compensation event, the situation is different, clause 63.1 of NEC3 says this:

The Contractor notifies the Project Manager of an event which has happened or which he expects to happen as a compensation event if

The Contractor believes that the event is a compensation event and

The Project Manager has not notified the event to the Contractor.

If the Contractor does not notify of 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 unless the Project Manager should have notified the event to the Contractor but did not

98. The FIDIC form contains similar provisions. Sub-clause 20.1³⁰ states that:

If the Contractor considers himself to be entitled to any extension to the Time for Completion and/or any additional payment, under any Clause of these Conditions or otherwise in connection with the Contract, the Contractor shall give notice to the Engineer, describing the event or circumstance giving rise to the claim. The notice shall be given 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.

³⁰ Clause 20.1 is identical in the Red, Yellow and Silver Books, except that in the Silver Book, the Employer performs the role of the Engineer.

If the Contractor fails to give notice of a claim within such period of 28 days, the Time for Completion shall not be extended, the Contractor shall not be entitled to additional payment, and the Employer shall be discharged from all liability in connection with the claim. Otherwise, the following provisions of this Sub-Clause shall apply.

99. That said, the regime very different between FIDIC and NEC. Under FIDIC, the duty is to notify of an *entitlement* to additional time or money; under NEC3 there is a duty to notify of an *event*.
100. Here, the *contractor must* notify the *Project manager* of an event which happens or which the *contractor* expects to happen if:
- (i) The *Contractor* believes the event is a compensation event, and
 - (ii) The *Project manager* has not notified the event to the *contractor*.
101. If the *Contractor* does not give notice within eight weeks of becoming aware of the event, the *Contractor* is not entitled to additional payment or any change to Completion Date or the Key Dates unless the *Project Manager* should have notified the event to the *Contractor* and did not.
102. This is a fundamental requirement of the NEC3. The *Contractor must* give notice of compensation events within eight weeks of becoming aware. This clause is a radical departure from the NEC Second Edition whereby notice had to be given within two weeks, but the NEC Second Edition was silent as to whether failure to give notice within this time would result in the *Contractor* being penalised.
103. The *Project Manager* has one week from receipt of the notification to decide that the event:
- (i) is the *Contractor's* fault/responsibility or has not happened and is not expected to happen;
 - (ii) has no effect on the cost of the *works*;
 - (iii) is not a compensation event.
104. If, however, the *Project Manager* decides that the matter is a compensation event, the *Project Manager* will notify the *Contractor* and instruct the *Contractor* to submit a quotation.
105. If the *Project Manager* did not give his decision within one week of the *Contractor's* notification, the *Contractor* can point out this failure to the *Project Manager*. If the *Project Manager* does not reply within two weeks of this later notification, then the event complained of is a compensation event and the *Contractor* is deemed to have been instructed to submit quotations.³¹
106. The *Contractor* must submit a quotation within three weeks of being instructed to do so. The *Project Manager* has two weeks to reply which must state:

³¹ See core clause 61.4

- (i) whether a revised quotation is needed;
- (ii) whether the quotation is accepted;
- (iii) whether the *Project Manager* will be making his own assessment;
- (iv) in the event of a proposed instruction, whether or not the *Project Manager* will actually be giving the proposed instructions.³²

107. If the *Contractor* is asked to provide a revised quotation, he has three weeks to do so again.

108. So, here is the fertile area for disputes. What if the contractor's notification is late?

109. The deadline does not necessarily start on the date of the claim event itself but on the date the contractor objectively should have become aware of the event. Whilst it is relatively easy to identify the claim event in the case of a single event such as the issuing of engineer's instructions or the receipt of borehole tests indicating unforeseen ground conditions, when, however, the claim event is a continuous event, such as, unforeseeable weather over a certain period of time, it can become extremely difficult to pinpoint the exact start of the period.

Is core clause 61.3 of the NEC3 a condition precedent?

110. Yes. Sub-clause 61.3 is a condition precedent and potentially provides the employer with a complete defence to any claim for time or money by the contractor not started within the required time frame.

111. Generally, in England and Wales, the courts will take the view that timescales in construction contracts are directory rather than mandatory, so that the contractor should not lose its right to bring its claim if such claim is not brought within the stipulated timescale.³³ In the case of *Bremer Handelgesellschaft mbH v Vanden Avenne Izegem nv*,³⁴ however, the House of Lords held that a notice provision should be construed as a condition precedent, if:

- (i) it states the precise time within which the notice is to be served, and
- (ii) it makes plain by express language that unless the notice is served within that time the party making the claim will lose its rights under the clause.

112. Sub-clause 61.3 plainly fulfils both these conditions as:

- (i) the notice of claim must be served within eight weeks of the contractor becoming aware of the event, and
- (ii) if the contractor fails to give notice of a claim within such period of eight weeks, he is not entitled to time or money.

³² Core clause 62.3

³³ *Temloc v Errill Properties* (1987) 39 BLR 30, (CA) per Croom-Johnson LJ

³⁴ [1978] 2 Lloyd's Rep. 113, (HL) per Lord Salmon.

113. Sub-clause 61.3 was thus clearly drafted as a condition precedent. However, there is always a possibility that a court/arbitral tribunal might decline to construe it as a condition precedent, having regard to the particular circumstances of the matter before it and the impact of the applicable law.

Are there any ways round clause 61.3 ?

114. Quite possibly not, at least in England and Wales.

Prevention

115. The concept of preventive acts is based on the universally accepted provision that one is not entitled to benefit from own wrongs. It thus operates to defeat the employer's claims for liquidated damages if, by its own acts or omissions, the employer has prevented the main contractor from completing its work by the date for completion, and thus rendered "time at large".
116. To protect its right to claim liquidated damages and to avoid the time for completion being declared "at large", the employer will therefore insert provisions into the contract enabling the contractor to seek an extension of the time for completion in case the employer is responsible for the delay incurred by the contractor.
117. The issue with conditions precedent to the contractor's right to claim for an extension of time, is that if the contractor fails to comply with such conditions, then its right to claim for additional time will be forfeit, and thus the question arises as to whether the employer will then still be able to claim liquidated damages (and arguably rely on its own wrong).
118. This issue was considered in 1999 in the case of *Gaymark Investments Pty Ltd v Walter Construction Group Ltd* in the Northern Territory of Australia,³⁵ where the court found that the "prevention principle" took precedence over the notification provisions, notwithstanding the fact that such provisions had clearly been drafted as a condition precedent. The employer was accordingly not allowed to claim for liquidated damages and the contractor not deprived of its right to claim for an extension of time in spite of its failure to serve a valid notice.
119. This judgment gave rise to a long debate as to whether the same principles should be applied in England & Wales and other common law jurisdiction. Whilst some commentators argued that a similar approach might be adopted,³⁶ others strongly rejected the reasoning of the court in *Gaymark*.³⁷
120. One author submitted that the better approach for resolving the tension between time-bar clauses and the prevention principle would be to accept first that the prevention principle is a rule of construction (as opposed to a rule of law) and can therefore be excluded by contractual provisions such as sub-clause 61.3, and second that the prevention principle does not apply

³⁵ (1999) 18 BCL 449, (2005) 21 *Construction Law Journal* 71.

³⁶ *Keating on Building Contracts* (8th edition 2006) at paragraph 9-025.

³⁷ Professor Ian Duncan-Wallace "Prevention and Liquidated Damages: a Theory Too Far" (2002) 18 *Building and Construction Law*, 82.

because the major cause of the contractor's loss in the above circumstances is the contractor's failure to operate the contractual machinery.³⁸

121. This second option was clearly accepted in 2001 by the Inner House of the Court of Session of Scotland in the case of *City Inns Ltd v Shepherd's Construction*,³⁹ in which Lord MacFadyen found that there was a causal connection between the contractor's failure to comply with the notification provisions of the contract and its liability to pay a sum of money which bears no relation to the loss resulting to the employer from that breach of contract. Lord MacFadyen thus held that the liquidated damages remained payable by the contractor:

on the basis that it is a genuine pre-estimate of the loss suffered by the employer as a result of the delay in completion, and is not converted, by the fact that the contractor might have avoided that liability by taking certain steps which the contract obliged him to take, but failed to do so, into a penalty for failing to take those steps. The fact that the contractor is laid under an obligation to comply with clause 13.8.1 [obligation to notify], rather than merely given an option to do so, does not in my opinion deprive compliance with clause 13.8.1 of the character of a condition precedent to entitlement to an extension of time. Non-compliance with a condition precedent may in many situations result in a party to a contract losing a benefit which he would otherwise have gained or incurring a liability which he would otherwise have avoided. The benefit lost or the liability incurred may not be in any way commensurate with any loss inflicted on the other party by the failure to comply with the condition. But the law does not, on that account, regard the loss or liability as a penalty for the failure to comply with the condition (The "Vainqueur José", per Mocatta J at 578, col. 2).

122. The crucial fact in this case was that, under the terms of the contract, but for its failure to serve a valid notice on time, the contractor would have been in a position to claim an extension of time and therefore defend the employer's claim for liquidated damages. The fact that it failed to comply with this simple requirement may lead to very harsh consequences such as the employer being able to claim liquidated damages despite being responsible for the delay incurred by the contractor. However, the contractor only had itself to blame for losing the right to claim additional time.
123. Six years after Lord MacFadyen's decision in *City Inns Ltd v Shepherd's Construction*, the position of the English courts with regard to the effect of the "prevention principle" on notification clauses was also finally clarified in the judgment of the TCC in *Multiplex Construction v Honeywell Control Systems*,⁴⁰ where Mr Justice Jackson held that:

"Whatever may be the law of the Northern Territory of Australia, I have considerable doubt that Gaymark represents the law of England. Contractual terms requiring a contractor to give prompt notice of delay serve a valuable purpose; such notice enables matters to be investigated while they are still current. Furthermore, such notice sometimes gives the employer the opportunity to withdraw instructions when the financial consequences become apparent. If Gaymark is good law, then a contractor could disregard with impunity any provision making proper notice a condition precedent. At his option the contractor could set time at large."⁴¹

³⁸ Hamish Lal *The Rise and Rise of "Time-Bar" Clauses: The "Real Issue" for Construction Arbitrators* (2007) ICLR 118.

³⁹ Outer House, Court of Session, CA101/00.

⁴⁰ [2007] EWHC 447 (TCC)

⁴¹ [2007] EWHC 447 (TCC) at para. 103.

124. The condition precedent did not render time at large. A condition precedent which bars a right to an extension of time if not complied with is valid.

Good faith and core clause 10.1

125. This is where core clause 10.1 comes in. In general terms the English courts are not, it has to be said, great fans of the concept of good faith, even if it is a contractual obligation. One reason for this is that it is not always that easy to define what good faith might mean. The English courts have said this:

It is a principle of fundamental justice that if a promisor is himself the cause of the failure of performance, either of an obligation due to him or of a condition upon which his own liability depends, he cannot take advantage of the failure.⁴²

126. It is possible that the concept of good faith can help defeat the harsh consequences of clause 61.3. However, the concept of time bars is also accepted and upheld even by the courts in civil law jurisdictions, provided they appear to be reasonable under the circumstances. As you would expect, everything would depend on the circumstances of the case and the conduct of both parties. If a contractor is only a few days late in submitting its notice in respect of very substantial claims and the forfeiture of its contractual rights would result in serious financial difficulties, then one might reasonably be entitled to argue that it would be contrary to good faith for the employer to rely on the condition precedent. Similarly, if the employer has actual knowledge of the "event or circumstance giving rise to the claim", and/or suffers no substantial harm as a result of not receiving the contractor's notice on time, then, having regard to its implied obligation of good faith, the employer may not be able to rely on sub-clause 61.3 to defeat the contractor's claims.
127. In practice, much will therefore depend on the circumstances of the case and the conduct of both parties. The contractual obligation to deliver timely notice of one's intention to claim additional time or money will normally be upheld, unless the particular circumstances of the case show that such conclusion would lead to a misuse of a right or a breach of the parties' good faith obligations.

Conclusion

128. His Honour Judge Coulson has conjured up a new character: the "resourceful litigant" who has been and will continue to be a major player in adjudication and adjudication enforcement cases. I suspect you will find him, insofar as NEC3 contracts are concerned, arguing the good faith point.

06 October 2007
Jeremy Glover
Fenwick Elliott LLP

⁴² *CIA Borcad & Panona SA v George Wimpey & Co* [1980] 1 Lloyd Rep 598