What is a Compensation Event (CE)?

If you've ever worked on an NEC Contract you would have heard the term Compensation Event (CE). If you haven't heard the term, you may have heard of Relevant Events, used on other contracts like JCT. This document will aim to provide clarity on Compensation Events and provide you with some practical examples.

> *"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" – Fenwick Elliot.*

The purpose of a CE is to place the contractor into the position he was in before the event occurred. In other words, if an event caused a contractor to lose £2,000, the CE would aim to reimburse the loss incurred. Alternatively, an event may cause a delay to the Completion Date or Key Date. A CE will aim to alter these dates, so the effect of the event has no impact how early or late a project or key date completion is met.

Disclaimer: The assumptions within this article are based on a non-amended NEC3 Engineering and Construction Contract. The clauses and project stakeholders will vary on different projects.

Examples of Compensation Events (NEC3)

This list gives examples of specific CEs from clause 60.1 of NEC3:

- The Employer does not allow access to the site by the access date shown on the Accepted Programme
- The Project Manager or Supervisor changes a decision which he has previously communicated to the contractor
- The Project Manager gives an instruction to stop or not to start any work, or changes a Key Date

Who owns the risk?

There are ways that a contractor can protect themselves when it comes to risk. Ensuring that each risk is allocated in some way is essential to ensuring the financial success of a project. For example, the risk of stolen plant could be counteracted by insurance, the risk of delayed material orders could be counteracted by adding risk into the construction programme and finally there could be risk which the contractor does not hold all together. This would be known as employer's risk. A list of what risk is held by an employer can be found in clause 80.1 (NEC3). Risk that is held by the employer is a CE under clause 60.1 (14).

Notification of Compensation Events and time bar (clause 61.3)

As soon as a contractor is aware of an event, he should issue a Notification of Compensation Event (NCE). If the contractor fails to do this within 8 weeks of becoming aware of the event then they are not entitled to a change in prices, completion date or a key date. Exception is placed on this rule if the event arises from a project manager or supervisor giving an instruction, issuing a certificate, changing an earlier decision or correcting an assumption.

Compensation Event Deadlines:

1. Contractor: 8 weeks to notify an event which may be a CE
2. Project Manager: 1 week to decide if they consider it is a CE
3. Contractor: 3 weeks to issue a quotation
4. Project Manager: 2 weeks to respond

It's not always that simple

Let's say you are a utilities contractor. You arrive on site, start digging and whoops. You hit concrete. You didn't think you'd be meeting Mr concrete today but it seems you have. There was no mention of this obstruction in the site information so you might be thinking this is a guaranteed CE. However, this isn't always the case. The legitimacy of the Compensation Event will depend on other factors external to the site information. First, let's look what the contract says (NEC3).

Clause 60.1 (12): *"**Physical Conditions** – The contractor encounters physical conditions which:-*

- *are within the site*
- *are not weather conditions*
- *an **experienced Contractor** would have judged to have such a **small chance** of occurring that is would have been unreasonable for him to have allowed for them"*

The last paragraph seems quite subjective right? What is an "experienced Contractor"? What is a "small chance"? If you find yourself in the situation where you have to argue this point then you need to ensure you've got a solid argument. If you were carrying out work in a city, it's going to be hard to justify your argument. A much better approach is to ensure this risk is allowed for within the price. It's easy to get lazy and assume any unexpected issues would be covered by a CE. However that assumption can lead to avoidable loss.

Conclusion

If you are ever working on an NEC contract it's imperative that Compensation Events are understood. This will ensure you claim for reimbursement you're entitled to and allocate risk for events which you are not entitled to. Failure to do so, could cause a contractor to suffer a financial loss from a project. The role of the Quantity Surveyor is to ensure that profit is maximised on projects and understanding Compensation Events is part of how this is achieved.