

Practice Note

Extension of time and variation entitlements

EXPLANATORY NOTE:



This Practice Note is a product of the Construction Industry Leadership Forum. It provides a principle-based strategy with options that are available to procuring agencies in response to the identified challenge. Implementation of options may necessitate change to existing government policy or procurement rules to give them broader application.

PRINCIPLE:

Provisions providing the contractor with relief/entitlements should:

- » preserve the client's legitimate interest in being properly informed:
 - > of potential claims/liabilities as they arise; and
 - > before being required to make a decision or take action (such as granting an Extension of Time (EOT), approving a costs claim, implementing mitigation measures or instructing a variation);
- » avoid provisions which undermine the risk allocation that was commercially agreed between the parties;
- » incentivise both parties to reach agreement, to the extent possible, on key metrics for the entitlement (scope, time and cost impact) prior to taking effect; and
- » provide for governance and decision making, recognising the benefit of the parties working together in good faith to reach agreement in a timely manner when issues arise.

Set out below are options available to address the principle as applicable to the particular circumstances of a project. The practices identified below should not be considered mutually exclusive. An approach could be to involve a mix of options. That mix could vary depending on contract type and procurement model.

CHALLENGES AND OPPORTUNITIES:

A. Governance/Leadership

There is a high level of complexity involved in managing and assessing contract claims for extensions of time and variations. These challenges require strong leadership and effective governance structures to be in place to reach a reasonable position for all parties. The benefit of simplifying contract administration can be far reaching, however it depends on the parties accurately reflecting their claim, proactive management, early and timely communication and leadership behaviours demonstrating a commitment to resolving issues. This leadership behaviour is a common theme applicable to all the options and practices below in this practice note.

Options

The practices outlined below should not be considered mutually exclusive.

PRACTICE

- 1 Include a clear issues resolution mechanism directed towards dispute avoidance, involving senior representatives with clear decision-making points, which requires parties to act in good faith towards an outcome focussed resolution in a timely manner.

B. Claims management

Overly prescriptive notice clauses with restrictive time bar periods can, in practice, become administratively burdensome and unmanageable for all parties in the supply chain (with notification periods necessarily diminishing further down the chain).

It can often take some time for the relevant personnel within a contractor to become aware of an event giving rise to a potential claim. If the contractor is required to give notice within 2 days of an event occurring (rather than being linked to awareness of the event), contractors can risk losing their legitimate entitlement before having become aware of its existence. These mechanisms require dedicated resources to administer and the effort needed to strictly comply can become a diversion of project resources from the core function of the project team.

Contractual regimes for claiming entitlements should seek to balance the legitimate interests of the client in being properly informed of, and able to assess, delays and claims within a reasonable time and fair, manageable processes enabling contractors to seek recourse for legitimate claims.

Options

The practices outlined below should not be considered mutually exclusive.

PRACTICE	
1	Government should consider the administrative burden imposed by a claims process. There should be joint ownership of the claims process with dedicated client and contractor responsibility.
2	Contractual mechanisms (suitable to the delivery model) should enable claims to be triggered when the contractor becomes aware or should reasonably have become aware, of the relevant delay or variation event (as distinct from when the event occurred).
3	Contractual regimes should be designed to ensure that contractors keep clients sufficiently informed about what is occurring on a site. Early warning provisions should ensure any issue which may give rise to a potential claim is addressed in real time.
4	Clauses which require contractors to provide significant amounts of detailed and costed information to the client within an extremely short period of time (with entitlements forfeited in the event of non-compliance) should be replaced with regimes which allow for staggered information flow, provided that all relevant information is ultimately provided within a reasonable time of the event having occurred.
5	Consider whether time bars should be replaced with a “claims horizon” concept whereby a contractor is only entitled to extensions of time and/or delay costs for circumstances or consequences occurring within a reasonable period preceding notification (as well as the period subsequent to notification). I.e. delayed claims do not eradicate the entitlement, just reduce it. Where strict time bars are retained, realistic periods for issue of notices and submission of claims should be included. E.g. final payment claims.
6	Government should consider whether a ‘Claims Register’ is a better alternative to the contractor being required to issue ongoing monthly notices where the event or claim remains unchanged since the previous month. Such a register should include a trigger for regular escalation of the claim to a senior or executive level forum to ensure that the parties are incentivised to address the claim in a timely matter rather than allowing claims to aggregate for resolution towards the end of the term.

C. Timely contract administration

Where the client fails to respond to contractor notices or there are no specified time periods within which the client is required to respond, it can be extremely difficult for the contractor to programme work and maintain schedule. Poor contract administration on the part of the project owner can result in poorer quality contract administration by the contractor and a worse outcome for the project overall.

Contractual regimes should be designed to incentivise robust and timely contract management practices by both contractor and client, including clear timeframes for engagement and/or response.

Options

The practices outlined below should not be considered mutually exclusive.

PRACTICE	
1	Government and contractors should develop training and capability in contract management to ensure their people can both negotiate and properly administer a contract that is consistent with the project's risk profile.
2	Project management teams should be incentivised (through training and appropriate KPIs) to comply with reasonable time periods for engagement and response.
3	Both parties should seek to ensure that teams responsible for contract administration and decision-makers in particular are staffed by employees or personnel with sufficient delegated authority to make binding decisions on behalf of that party.
4	There should be clearly defined decision points within a claims process, and early escalation processes for quick resolution of issues relating to claims.

D. Ensuring objectivity in claims assessment

Where the client is provided with discretion regarding the assessment or granting of entitlements, the client is not always required to act reasonably and, in many cases, the contract reserves the client's right to act in its absolute discretion. This reduces the contractor's confidence that administration of the contract will produce fair and properly considered outcomes, which can drive more adversarial behaviours observed through bypassing of contractual processes and the rapid escalation of disputes.

Options

The practices outlined below should not be considered mutually exclusive.

PRACTICE	
1	Contracts should have clear and objective criteria for entitlements. To the extent that discretionary rights for the client are to be included, the client should be required to act reasonably in exercising those rights and both parties should be encouraged to behave cooperatively and in good faith.
2	Where the client does not comply with contractual time periods when responding to a particular claim under contract, the client should not be entitled to strictly enforce contractual time bars against the contractor in respect of the same claim.

E. Addressing impacts of delays not on the critical path

Delays caused by risks retained by the client do not always result in an extension of time being granted if, for example, the contract requires that delay caused by the client must be on the critical path before an EOT is granted. However, substantial cost can nevertheless be incurred even where the relevant delay is not to a critical path activity and the completion date is not affected. For example, a complex multi-site project may experience delays for client-retained risks at non-core sites which do not of themselves impact the critical path but which nonetheless cause substantial disruption costs for the contractor. Regimes which disentitle the contractor from claiming any cost recovery in these circumstances do not always reflect the true commercial intent behind the risk allocation.

There should be a balance between ensuring that claims are not made for minor and manageable delays not materially impacting on time and cost, while acknowledging that some non-critical path delays can still have a material cost impact on the contractor.

Options

The practices outlined below should not be considered mutually exclusive.

PRACTICE

- 1** Contractors should not be prohibited from recovering disruption or delay costs arising from client caused (or retained risk) disruption or delay irrespective of whether a critical path activity or the end completion date is impacted. To achieve this, a threshold-based hurdle could be included for non-critical path delay costs claims.
- 2** On large scale projects, Government should consider whether separable portions can be created, each with specific milestones relevant to the administration of time and cost entitlements arising from disruption or delay.

F. Variations

In contracts where a significant number of variations arise, neither party is typically resourced to finalise those variations within the requirements of the usual variation regimes that apply. Both parties therefore risk inadvertently waiving legitimate interests or increasing the risk of disputes at a later stage.

Where variations are initiated by the client, but not resolved promptly, it is often the case that the contractor must fund the variation until its variation claims are resolved.

Responding to client requested variation proposals can require a contractor to incur significant cost in preparing a preliminary design and costing the finished design and physical works. However, the client then has the discretion whether or not to elect to instruct that variation and, where it does not, the contractor does not always have an entitlement to recover its costs.

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PRACTICE	
1	Where there is potential for a lot of scope growth and/or change, other collaborative delivery models may be more appropriate than traditional D&C and PPP contracts. Regardless of the delivery model, contractual mechanisms (suitable to the delivery model) should be structured in a way which respond appropriately to changes.
2	Minor variations (which individually may have little effect, but when accumulated can have a considerable effect) should be addressed through a process that logs them as variations and then aggregates them. For the sake of efficiency these can be valued in batches (of an agreed value threshold).
3	A fast track contractual process should be implemented to ensure that variations are promptly resolved before considerable expenditure is required to be incurred.
4	The variation regime should consider the burden on the contractor in preparing variation proposals and allow for the contractor to recover reasonable costs associated with the preparation of responses to client requests for variations (whether or not the variation proceeds) where the burden is significant.