

MDA PRESENTS



FIRST AID FOR CONTRACTS



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TERMINATION UNDER NEC3 (APRIL 2013)

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We are living in unprecedented times. The national lockdown introduced by Government on 27 March 2020 was a curveball unexpected by almost every industry and has left the country reeling from its severe and long-lasting effects.

The Construction industry was not spared as only those industry players who were classed as “essential services” were able to work uninterrupted. For the rest, the start-up since 1 May 2020 has been staggered and slow and the final re-opening of the sector on 1 June 2020 heralded severe impacts on the viability and affordability in continuing with certain projects. We are, as is to be expected, seeing termination of contracts on the rise as our current economic climate is considered the worse crisis South Africa has faced in a century.

Due to this rising industry trend, we take a look at termination under the NEC3 (April 2013) contract.

Under the NEC3, Core Clause 9 [TERMINATION] allows for circumstances where either party may terminate the Contractor’s obligation to provide the Works. Hence, there is no separate clause depending on which party seeks to terminate.

Sub clause 91 provides 21 general reasons for termination. Reasons vary from material breaches of contract to insolvency/bankruptcy to delayed payment by the Employer. The Termination Table included in sub clause 90.2 contain 14 reasons the Contractor may rely on to terminate. The Employer may terminate for any reason. Incidentally reason 21, termination for a force majeure event, is only available to the Employer.

A specific procedure is to be followed by the party resorting to termination, which procedure is dependent on the reason for termination and determined by reference to the Termination Table.

The Termination Table further details when termination payments will flow from the termination.

A party who wishes to terminate must ensure that it is relying on the correct reason/s and has sufficient proof (in the form of documents/records) to warrant a termination under clause 91. A wrongful termination or following the incorrect procedure to terminate could amount to repudiation of the contract by the party wishing to terminate who then potentially faces the risk of a claim by the other party.

Whilst the reasons (R1 to R10 – the bankruptcy/insolvency grounds) do not require any default notice to be issued, reasons R11 – R15 (Contractor default) contain a pre-requisite that the Project Manager has notified the Contractor of his default. Where this default has not been rectified within 4 weeks of the notification, a notice of termination may be issued.

Sub-clause 90.1 which reads as follows:

*“If either Party wishes to terminate the **Contractor’s** obligation to Provide the Works he notifies the **Project Manager** and the other Party giving details of his reason for terminating. The **Project Manager** issues a termination certificate to both Parties if the reason complies with this contract”*

essentially places a confirmatory role on the Project Manager who will ensure that the reason for termination is valid in the circumstances. Once the Project Manager has verified the applicable grounds, he will issue a termination certificate. Thereafter the Contractor does nothing further to Provide the Works.

Reference to the Termination Table contained in sub-clause 90.2, the terminating party and the reason for termination, prescribes which combination of the four procedures (P1, P2, P3 or P4) will apply. The four procedures as detailed in sub-clause 92 are set out below:

P1	On termination, the <i>Employer</i> may complete the <i>works</i> and may use any Plant and Materials to which he has title (P1)
P2	The <i>Employer</i> may instruct the <i>Contractor</i> to leave Site, remove any Equipment, Plant and Materials from the Site and assign the benefit of any subcontract or other contract related to performance of this contract to the <i>Employer</i> .
P3	The <i>Employer</i> may use any Equipment to which the <i>Contractor</i> has title to complete the <i>works</i> . The <i>Contractor</i> promptly removes the Equipment from Site when the <i>Project Manager</i> notifies him that the <i>Employer</i> no longer requires it to complete the <i>works</i> .
P4	The <i>Contractor</i> leaves the Working Areas and removes the Equipment.

The aforementioned procedure will follow immediately the termination certificate has been issued. A successful termination always entitles an Employer to complete the Works and in certain instances to utilise the Contractor’s Equipment to do so.

Similarly, by reference to the Termination Table, the terminating party and the reason for termination, determines which combination of the four amounts may become due to the terminating party (A1, A2, A3 or A4). Sub clause 93 provide details of the four amounts as follows:

Sub-clause 90.4 provides that the Project Manager will within thirteen weeks of termination, certify a final payment to or from the Contractor – this amounts to the Project Manager’s assessment of the amount due on termination (less previous payments to the Contractor). The amount due always includes the A1 component and one or more of the others.

The prevailing state of the industry post the national lockdown renders reason 20 (the project manager instructing the contractor to stop work and not start again within 13 weeks, not due to a default by either party) or reason 21 (an event occurs that stops the contractor completing the works for more than 13 weeks) common-place grounds for termination.

A1	<p>The amount due on termination includes:</p> <ul style="list-style-type: none"> • an amount due assessed as for normal payments, • the Defined Cost for Plant and Materials <ul style="list-style-type: none"> ○ within the Working Areas or; ○ to which the <i>Employer</i> has title and of which the <i>Contractor</i> has to accept <i>delivery</i>, • other Defined Cost reasonably incurred in expectation of completing the whole of the <i>works</i> • any amounts retained by the <i>Employer</i> and • a deduction of any un-repaid balance of an advanced payment.
A2	The forecasted Defined Cost of removing the Equipment.
A3	A deduction of the forecast of the additional cost to the <i>Employer</i> of completing the whole of the <i>works</i>
A4	<p>The <i>direct fee percentage</i> applied to</p> <ul style="list-style-type: none"> • for Options A, B, C and D, any excess of the total of the Prices at the Contract Date over the Price for Work Done to Date or • for Options E and F, any excess of the first forecast of the Defined Cost for the <i>works</i> over the Price for Work Done to Date less the Fee.

In both these situations however, the Contractor should have notified a compensation event under either sub-clause 60(4) or 60(19) which entitles the Contractor to additional time and costs. Should termination occur, this additional cost is to be included in the Project Manager's assessment. The Contractor will also receive the A1 and A2 amounts. Where reason 20 or 21 are relied upon for termination, the Employer cannot recover from the Contractor additional costs incurred to complete the works (A3). The Employer is entitled to the A3 sum only in the event of the Contractor's insolvency or default. The fee percentage applicable to the remainder of the work (A4 sum) is applicable where the Employer terminates at will or where the Contractor terminates for insolvency or default by the Employer.

Payment follows within three weeks of the Project Manager's certificate.

This termination clause can be viewed as well-constructed as it ensures clarity to both parties from the onset of the Contract the specific circumstances which will allow them to terminate, the procedure to follow to terminate and the payments that will flow under different scenarios. Thus, an innocent party is able to ascertain what may be recoverable through termination. Further, by providing time frames for the final certificate and payment thereof, the clause leaves no uncertainty and safeguards the innocent party in recovering its losses.