



ARTICLE: Good things come to those who wait – Construction Act amendments: implications for construction contracts

The amendments to the Housing Grants, Construction and Regeneration Act 1996 (the “Construction Act”¹) came into force on 1 October 2011 (in England and Wales) and will be in force from 1 November 2011 (in Scotland). The changes have been a long time coming and are the product of waves of consultation spanning several years.

The changes will apply to any construction contract² *entered into on or after 1 October 2011*. The new changes will not be retrospective: any contract entered into before 1 October 2011 will continue to be governed under the old HGCRA regime.

This will mean that for some time the construction industry will be operating two sets of rules depending on when any one contract was entered into.

New standard form contracts and subcontracts are to be published, the JCT having already published a change track version of JCT 2005 – JCT 2011, showing the changes to be made.

We set out below the main areas where the HGCRA is to be amended.

Removal of requirement for construction contracts to be in writing

The provisions of the HGCRA only applied to construction contracts in writing or evidenced in writing. It was the commonly held view across the construction industry when consultation on the new Act began that this requirement should be reviewed. The Construction Act will apply to all construction contracts whether they are in writing, oral or partly oral. This means that contracts that are partly in writing or oral can now be referred to statutory adjudication. The Act provides however that the adjudication provisions of a contract must be in writing, failing which the adjudication provisions of the Scheme³ will apply.

Whilst this will do away with the old arguments over whether all of the contract terms have been recorded in writing, new areas of dispute will surface, such as what are the oral terms that have been agreed and is there a contract at all. This could mean more witness evidence and hearings to enable the adjudicator to form a view on the terms agreed, which could result in an increase in costs and lead to more extensions of the period for deciding the dispute beyond 28 days. However, many adjudicators already manage the procedure in this way and reach decisions on such issues so the impact of these changes may not be that great.

Changes to Payment Provisions

It is the changes made to the payment provisions under a construction contract that are the meat of this new legislation.

As always the devil is in the detail and it will be important for all parties operating under the new regime to get to grips with the revised procedures.

Adequate mechanism for determining what payments become due

Construction contracts will still have to meet this requirement, however this will no longer be satisfied if the contract makes payment conditional on either:

- (a) The performance of obligations under another contract;
- (b) A decision as to whether obligations under another contract have been performed; or
- (c) The date on which payment is due being dictated by the giving by the payer of a notice to the party to whom payment is due.

This will outlaw “pay – when- certified” clauses and the type of provision where the payer effectively dictates the due date for payment will be what it says it is.

The new provision is good news for sub – contractors who will no longer be in the position of waiting (sometimes indefinitely) for the second half of their retention to be released (which under many sub – contract forms is not due until after issue of the certificate of making good defects under the main contract).

The prohibition will not apply to management contracts and pursuant to Exclusion Orders⁴ to situations where a party to a PFI contract has subcontracted its construction obligations (PFI agreements remain excluded from the entirety of Part 2 of the Construction Act).

Payment Notices

The new Construction Act requires contracts entered into on or after 1 October 2011 to provide that:

- Either the paying party (or architect or contract administrator) or the payee must give a *payment notice* no later than 5 days after the payment falls due, setting out the sum they consider to be due and the basis upon which that sum is calculated.
- The payment notice must be served even if the sum is zero.
- If the contract requires the paying party (or architect or contract administrator) to serve the payment notice, but no notice has been provided, the payee may issue a payment notice once the time when the payer should have issued its notice has expired. However, if the contract already permits the payee to issue a payment notice (ie an application for payment) that application will stand as the payment notice and the payee will not be permitted to serve a second notice.

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- If under the contract the payee is to serve the payment notice and fails to do so, there will be no entitlement to that interim payment.
- Where a notice is served by the payee because the payer has failed to issue a notice, the final date for payment is pushed back by the same number of days as the period between the date the paying party should have served its notice and the date on which notice was actually given by the payee.
- The payer must pay the “*notified sum (to the extent not already paid) on or before the final date for payment*”: the “*notified sum*” is the amount indicated in the relevant payment notice.
- The requirements for withholding notices are changed and replaced with *pay less notices*. If a payer wishes to give notice of its intention to pay less than the notified sum it may do so: such notice must specify the sum the payer considers to be due (on the date it is served) and the basis on which that sum is calculated. A pay less notice must be given no later than the period prescribed in the contract and the default position under the scheme is the same as for withholding notices, namely notice must be given no later than 7 days before the final date for payment.

Care will be needed when operating under the new regime, particularly by employers, who must now live with the fact failure to issue the required payment notice (including as provided in the new JCT 2011 design and build contract failure to give notice on time or in adequate detail) will leave the way open for the contractor to issue its own notice or rely on its application for payment, and in the absence of a subsequent pay less notice, the employer will have to pay the amount requested by the contractor.

Insolvency

Under the new Act where a contract provides that if the payee becomes insolvent the payer need not pay any sum due, the payer need not pay *provided* the payee becomes insolvent *after* the time for issue of a pay less notice has passed. The right to withhold money after a contractor becomes insolvent must therefore be written in to the contract otherwise this provision will not bite.

Suspension

The rights afforded to contractors to suspend work in the event of non – payment have been extended to make clear that a contractor may operate this right in relation to *part only* of the works and to provide the contractor has the statutory right to recover a reasonable amount by way of the costs and expenses that he may incur in stopping work (such as demobilisation and remobilisation costs) - this is additional to the existing right under the HGCR to an extension of time in respect of the suspension.

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Adjudication Procedure

The requirement to include in construction contracts an adjudication procedure that meets the statutory requirements is unchanged, except that all construction contracts must include such provisions in writing, and failure to do so will mean the Scheme applies in default.

There have been some changes to adjudication procedure, in particular the requirement in the amended Scheme that the 28 (or where extended 42) period (unless agreed otherwise by the parties) allowed for the adjudicator to reach a decision will be calculated *from the date that the referral notice is received*.

The new Act introduces a '*slip rule*' which is a specific provision to enable the adjudicator to correct a decision to remove any clerical or typographical errors.

Costs in Adjudication

The HGCR did not address the matter of the parties costs of adjudication: this led to the practice by some of including so – called 'Tolent' clauses⁵ in their contracts, which more or less provided that all adjudication costs and expenses would be borne by the party referring a dispute to adjudication (irrespective of the outcome). The courts had begun to address this problem with such clauses being held to be onerous and inconsistent with the HGCR⁶.

The new Act outlaws the use of such agreements as to adjudication costs except where the parties agree on the allocation of costs *after* the notice of intention to refer the dispute has been given and this agreement is set out in writing.⁷ The adjudicator retains the power to apportion as between the parties payment of his or her fees and expenses.⁸

Actions

- Review all tenders, prospective contracts and contracts being procured and if these are to be entered into on or after 1 October 2011 they must comply with the new rules.
- Review standard terms and conditions, standard offer letters and contract documents so that they are compliant with the new Construction Act.
- That new standard forms, such as the new 2011 suite published by the JCT, are used with effect from 1 October 2011.
- Staff responsible for administering contracts on a daily basis should be familiar with the new rules and properly trained so as to avoid any costly errors.
- Review current contracts, such as framework agreements: any contract let under a framework on or after 1 October 2011 will need to be compliant with the new Act.
- Keep track of those contracts that are still operating under the old rules (ie those entered into prior to 1 October 2011) and contracts under the new Act: they will have different payment regimes.

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This bulletin is not definitive and as such cannot constitute legal advice. If you would like any further information or specific advice on the above please contact either Richard Silver on 0845 345 1244, Sarah Shemmings on 0845 345 1244 or Robert Shawyer on 02920 474 570.

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1. Part 8 of the Local Democracy, Economic Development and Construction Act 2009.
 2. "construction contract" is defined in s104 (1) of the HGCRA.
 3. Regulations amending the Scheme for Construction Contracts (England) have been published and should come in to force on 1 October 2011 alongside the revisions to the Construction Act.
 4. Construction Contracts (England) Exclusion Order 2011 and the Construction Contracts (Wales) Exclusion Order 2011, SI 2011/1713.
 5. *Bridgeway Construction v Tolent Construction* (2000) CILL 166.2
 6. *Yuanda (UK) Co Ltd v WW Gear Construction Ltd* [2010] EWHC 720 (TCC).
 7. Some commentators are critical of the drafting of the new legislation on this issue and submit there is a lacuna in the drafting that means the new Act does not succeed in totally outlawing "Tolent" type clauses: the Department for Business Innovation and Skills ("BIS") does not accept there is any ambiguity. It remains to be seen whether this will be an issue that comes before the courts.
 8. Scheme for Construction Contracts Part 1 (Adjudication) paragraph 25 as amended at 3 (13) of the draft Scheme for Construction Contracts (England) Regulations (Amendment) 2011.

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