

A close-up, artistic photograph of a stack of coins, likely British pounds, showing the texture of the metal and the edges of the coins. The lighting is dramatic, highlighting the metallic sheen and the intricate details of the coin's design.

dti

**IMPROVING PAYMENT
PRACTICES IN THE
CONSTRUCTION INDUSTRY**

2nd Consultation on
proposals to amend
Part II of the Housing
Grants Construction and
Regeneration Act 1996
and the Scheme for
Construction Contracts
(England and Wales)
Regulations 1998

JUNE 2007



Llywodraeth Cynulliad Cymru
Welsh Assembly Government

Improving payment practices in the construction industry: 2nd Consultation on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996

This is the second public consultation¹ seeking views on proposals drawn from Sir Michael Latham's report on the operation of Part II of the Housing Grants, Construction and Regeneration Act 1996 (the Construction Act) and the Scheme for Construction Contracts (England and Wales) Regulations 1998 (the Scheme). Having previously consulted on a broad range of issues, this consultation sets out the specific proposals we are making.

Issue Date: 20 June 2007

Response Deadline: 17 September 2007

Enquiries and responses to:

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¹ The first consultation, *Improving payment practices in the construction industry – consultation on proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 and Scheme for Construction Contracts (England and Wales) Regulations 1998*, was published in March 2005.

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Foreword

**By Rt. Hon Margaret Hodge MP MBE,
Minister of State for Industry and the Regions**

I know how important it is for all stakeholders that we have a system which delivers fair payment practices. We have made progress over the last decade but we have promised further improvements in the legislative framework.

It has taken a long time to reach this point but I am delighted that I am now able to issue this second consultation paper on proposals to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and the Scheme for Construction Contracts (England and Wales) Regulations 1998.

We originally wanted to introduce these changes through a Legislative Reform Order under the Legislative and Regulatory Reform Act 2006. That has not proved possible. We will therefore use primary legislation to enact these proposals and are currently examining a range of options to secure the earliest legislative opportunity. This enables us to consult on a full package of measures to:

- improve transparency and clarity in the exchange of information relating to payments, thereby enabling parties to construction contracts to manage cash flow better; and to
- encourage parties to resolve disputes by adjudication.

The proposals are not radical. They are intended to be proportionate amendments to the existing framework. We have only considered further legislative intervention where we believe it is absolutely necessary to achieve the aims of the original legislation – guidance must remain our preferred option to improve the operation of construction contracts.

Sir Michael Latham (both in the foreword to “Constructing the Team” and in his 2004 report to Nigel Griffiths) quoted the Dodo in *Alice’s Adventures in Wonderland* – “everybody has won and all must have prizes”. That remains the right background against which to consider the proposals in this document. Taken as a whole, any package of amendments we take forward must benefit all in the industry and its clients.

I look forward to a healthy discussion and a constructive response.



**Endorsement by Andrew Davies AM,
Welsh Assembly Government Minister for Social Justice
and Public Service Delivery**

There is no single easy answer to the problems associated with construction contracts. However, following the 2005 consultation exercise: *Improving payment practices in the construction industry* the responses received from the industry provided sufficient evidence that the existing regulatory framework makes a valuable contribution to fairness in the way construction contracts are agreed and operated.

356 responses to the 2005 consultation also showed that there was a high level of interest and support to amend Part II of the Housing Grants Construction and Regeneration Act 1996 and The Scheme for Construction Contracts (England And Wales) Regulations 1998 from the construction industry and its stakeholders.

Building on the first consultation, the proposals in this second formal public consultation provide the detail of the specific amendments we are seeking to make to the Construction Act to improve the statutory framework for construction contracts and improve communication between the parties on issues relating to payment.

The proposals on which we are now consulting will create a better, more focused and effective regulatory framework. They are intended to support the current effectiveness of the Construction Act and the fine balance between the range of interests it has been able to strike. They represent a focused set of amendments which are designed to address specific weaknesses which have been identified in the current operation of the Act.

Andrew Davies

Executive Summary

Background

The Review of the Construction Act was announced in the 2004 Budget.

Nigel Griffiths, then Parliamentary Under Secretary of State for Construction, Small Business and Enterprise, asked Sir Michael Latham to undertake a review of the Act.

Sir Michael's report was published in September 2004. It concluded that the Construction Act was generally working well but that some improvements would be helpful. According to various industry surveys, poor payment practices continue to be a major issue for many in construction.

In March 2005 DTI and the Welsh Assembly Government published a joint consultation paper – *Improving payment practices in the construction industry*. In January 2006 we issued a consultation analysis which set out our proposed way forward. During the remainder of that year, working with Sir Michael Latham and other members of a DTI appointed sounding board, we developed detailed proposals.

As stated in our analysis of the consultation, we had hoped to introduce proposals using a Legislative Reform Order under the Legislative and Regulatory Reform Act 2006. We have now concluded that it would be more appropriate to introduce these proposals using primary legislation. This consultation covers these primary legislative proposals in detail as well as the consequential amendments that will need to be made to the Scheme for Construction Contracts (England and Wales) Regulations 1998.

We will be seeking to introduce legislation to implement the proposals emerging from this consultation when Parliamentary time allows.

Proposals

We believe prompt and fair payment practice throughout construction supply chains will better enable the industry to adopt integrated working as the norm.

We are proposing to:

- improve transparency and clarity in the exchange of information relating to payments to enable the better management of cash flow;

- encourage the parties to resolve disputes by adjudication, where it is appropriate, rather than by resorting to more costly and time consuming solutions such as litigation; and
- improve the right to suspend performance under the contract.

We are proposing to do this by:

On adjudication

- improving access to the right to refer disputes for adjudication by:
 - applying the legislation to oral and partly oral contracts
 - preventing the use of agreements that interim payment decisions will be conclusive to avoid adjudication on interim payment disputes
- ensuring the costs involved in the process are fairly allocated

On payment

- preventing unnecessary duplication of payment notices
- clarifying the requirement to serve a section 110(2) payment notice
- clarifying the content of payment and withholding notices
- ensuring the payment framework creates a clear interim entitlement to payment
- prohibiting the use of pay-when-certified clauses

On suspension

- improving the statutory right to suspend performance by allowing the suspending party to claim the costs and delay that result.

This is not wholesale reform. These proposals are intended to be proportionate amendments to the existing framework to address specific issues that have arisen during the nine years the Construction Act has been in operation. Guidance remains the preferred route to improve the operation of construction contracts and we have only considered further legislative intervention where we believe it is absolutely necessary.

We are now seeking the views of the construction industry and its clients, through this consultation process, on:

- whether this package of proposals properly and adequately addresses the weaknesses in the existing framework; and
- how we might evaluate the costs and benefits of the package.

How to respond to this consultation

A consultation response form is at Annex D. It contains questions on each section of this consultation paper. Where a particular issue or proposal is of specific interest or concern to you, please feel free to make as many additional comments or suggestions as you feel appropriate.

The questions on regulatory impact are important as they will help us to carry out the Impact Assessment that will be needed if we go forward with legislation. Detailed and reliable information has been very hard to come by and, while we appreciate that this may be difficult, we should be very grateful if you would answer as many of these questions as you are able to. Your responses will enable us to assess whether the proposals deliver better payment practices than the legislation as it currently stands.

The consultation response form also covers the amendments that will need to be made to the Scheme for Construction Contracts (England and Wales) Regulations 1998. Generally we intend only to make minimal consequential amendments to the Scheme. However where we believe we have exercised some discretion in policy terms as to how to amend the Scheme, we have included questions on the proposals in the response form.

When responding, please state whether you are responding as an individual or representing the views of an organisation. If responding on behalf of an organisation, please make it clear who you are representing.

This is a joint consultation between the DTI and the Welsh Assembly Government. The Welsh Assembly Government has responsibility for policy on the construction industry in Wales. The amendments to the Scheme in Wales will be taken through the Welsh Assembly by the Welsh Assembly Government. If you are aware of any issues related to these proposals which have a specific impact in Wales we should be grateful if you would explain.

Though we cannot respond individually to each response we will publish an analysis of the consultation following completion of this exercise.

Response address

An electronic version of the consultation response form will be available from the construction pages of the DTI website.

<http://www.dti.gov.uk/sectors/construction/constructionact/page13956.html>

A response can be submitted by email using the form on the DTI website or by letter to:

Lilly Lotay

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We will not be able to accept responses after the consultation deadline.

Additional copies

You may make copies of this document without seeking permission. Further printed copies of the consultation document can be obtained from:

DTI Publications Order Line
ADMAIL 528
London SW1W 8YT

Tel: 0845-015 0010

Fax: 0845-015 0020

Minicom: 0845-015 0030

www.dti.gov.uk/publications

The Department will be able to arrange for this consultation to be made available in other languages or in Braille if required.

Further copies of the electronic consultation document can be obtained from the DTI website at www.dti.gov.uk/consultation

Confidentiality

Your response may be made public by the DTI or Welsh Assembly Government and will be shared with the Scottish Executive. If you do not want all or part of your response or your name made public, please state this clearly in the response. Any confidentiality disclaimer that can be generated by your organisation's IT system or included as a general statement on your fax cover sheet will be taken to apply only to information in your response for which confidentiality has been requested.

Access to information held by or on behalf of DTI is governed by the Freedom of Information Act 2000. Any requests for information received by DTI in relation to this Consultation will be administered accordingly. We handle any personal data you provide appropriately in line with the Data Protection Act 1998.

Help with queries

Questions about the policy issues raised in the consultation document should be addressed to:

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Questions about the involvement of the Welsh Assembly Government in the consultation process and future implementation should be addressed to:

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Rhydcar
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Tel: 01685 729 229

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Email: philip.gardiner@wales.gsi.gov.uk

Questions about the policy on the Construction Act in Scotland should be addressed to:

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If you have comments or questions about the way in which this consultation has been conducted, these should be sent to:

Kathleen McKinlay

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A copy of the Cabinet Office Code of Practice on consultation is contained in Annex B.

Introduction

Construction is one of the pillars of the UK economy. In England and Wales it accounts for 8.1% of national gross value added. Its economic importance is wider. Well managed and successfully delivered construction projects improve public services (health, education and transport), business productivity (offices, communications and retail) and housing and cultural and public spaces.

There are over 185,000 enterprises active in construction contracting and consulting in England and Wales, of which 99% are small or micro enterprises. The sector employs 1.3 million people. Characteristically profit margins in the industry are low and insolvencies are high compared to the economy as a whole. The supply team on a construction project often includes a large number of firms.

The context for the Construction Act was originally set by Sir Michael Latham's 1994 report *Constructing the Team*. Latham's overall approach to improving the performance of the construction industry – greater collaboration and integration – was subsequently reinforced by Sir John Egan in *Rethinking Construction* (1998) and *Accelerating Change* (2002) and most recently by the *2012 Construction Commitments* (2006). A successful, collaborative commercial arrangement cannot be supported by poor payment practices.

The Construction Act

Since coming into force on 1 May 1998, a number of difficulties have come to light and concerns have been raised about the effectiveness of the Construction Act. These have been the catalyst for the current review.

How the Act Works?

The Construction Act has two main aims:

- to ensure prompt cash flow; and
- to allow swift resolution of disputes by way of adjudication.

The Act currently achieves this by –

- Providing a statutory right to refer disputes to adjudication.
The adjudicator's decision is binding until finally determined by legal proceedings or arbitration (where there is an arbitration agreement) [section 108]
- Providing the right to interim, periodic or stage payments [section 109]

- Requiring that contracts should provide a mechanism to determine what payments become due and when, and a final date for payment [section 110(1)]
- Requiring that the payer gives the payee early communication of the amount he has paid or proposes to pay [section 110(2)]
- Providing that the payer may not withhold money from the sum due unless he has given an effective withholding notice to the payee [section 111]
- Providing that the payee may suspend performance where a sum due is not paid in full by the final date for payment [section 112]
- Prohibiting pay when paid clauses which link payment to payments received by the payer under a separate contract [section 113]

Other sections of the Act do the following –

- Define the scope of construction contracts [section 104]
- Define the meaning of construction operations including exemptions [section 105]
- Exempt residential occupiers [section 106]
- Restrict the application of the Act to contracts in writing [section 107]
- Provide a power to make a scheme for construction contracts [section 114]
- Make provision on service of notices, calculation of periods of time and application to the Crown [sections 115 – 117]

Background to this consultation

The Review of Construction Act was announced by the Chancellor in the Budget in March 2004:

“Following concerns raised by the construction industry about unreasonable delays in payment, the government will review the adjudication and payment provisions of the Housing Grants Construction and Regeneration Act in order to identify what improvement can be made.”

Nigel Griffiths, then Parliamentary Under Secretary of State at the DTI, asked Sir Michael Latham to review the legislation. Sir Michael’s findings were published in September 2004. His report concluded that the Construction Act is generally working well but some improvements would be helpful if means could be found to deliver them without adverse impacts on other parties or other elements of payment processes.

Following the publication of Sir Michael Latham’s report, the Government published a consultation paper, *Improving payment practices in the construction industry*, in March 2005. This first consultation document considered a number of proposals under the following headings.

- Improving the ability of parties to a construction contract to reach agreement on what should be paid and when
- Improving the ability of parties to a construction contract to manage cash flow and enable completion of work on the project
- Reducing disincentives to referring disputes to adjudication

Consultees were asked:

- whether the right issues had been identified;
- whether the right solutions had been proposed or whether there were other options; and
- how we might evaluate the potential costs and benefits of the different proposals.

The 356 responses demonstrated a high level of interest and support for the continued regulation of construction contracts and for the process of improving the current framework. Many were based on standard templates produced by the construction umbrella bodies. Others engaged in a detailed discussion of the proposals.

An analysis of the consultation responses was published in January 2006.

Since then we have:

- held an industry post consultation event;
- held a series of discussions with a sounding board of key industry figures; and
- conducted an informal consultation with the Construction Umbrella Bodies Adjudication Task Group

to develop this more detailed consultation on specific proposals.

In considering the responses to this consultation we will be continuing to keep in mind

- The need for improvement in payment practices under the legislation for all concerned.
- The need to respect the principle of freedom of contract, keeping intervention only those situations where it is deemed essential.
- The possibility of guidance to address certain issues as an alternative to regulation.
- The continuing development of case-law on adjudication and the payment provisions of the Construction Act.

Chapter I – Adjudication framework

1. **Removing the requirement that the Construction Act should only apply to contracts in writing**

Background

Currently the Construction Act only applies to contracts in writing. This requirement is defined broadly to include an agreement “recorded in any form”. As interpreted by the courts², the requirement is applied to all the non-trivial terms of the agreement. This creates grounds for the adjudicator’s jurisdiction to be challenged.

The effect of this can be as follows.

A dispute is referred to adjudication under the Act and one of the parties alleges that a contractual provision is not in writing (or that the contract has been varied by an oral agreement).

The adjudicator can then either decide that:

- the contract is in writing and he has jurisdiction, or
- that not all the agreement is in writing and he does not have jurisdiction.

Where the adjudicator decides he has jurisdiction he will continue with the adjudication. His decision however will not be enforced on an application for summary judgement if the court considers that the adjudicator did not have jurisdiction or that there is an arguable dispute as to his jurisdiction.

Where the adjudicator decides he has no jurisdiction, the adjudication of the dispute will come to an end.

Either outcome involves time and expense, not least the consideration of the challenge itself.

² See RJT Consulting Engineers Ltd-v-DM Engineering (NI) Ltd (2002) EWCA Civ 270, 8 March 2002

Current legislation

Section 107 has the following structure –

Section 107(1) – Restriction of the application of the Act to contracts in writing. Any other agreement is also only effective for the purposes of the Act if agreed in writing.

Section 107(2) – Definition of an agreement in writing (Section 104 states that a construction contract is an agreement). The courts have found that all three of the possible ways in which an agreement might be in writing must apply to the whole agreement (i.e. all of the contract terms must be in writing, agreed in a written exchange or “evidenced” in writing).

Section 107(3) – An agreement by reference to written terms is an agreement in writing.

Section 107(4) – An agreement recorded by a party or third party with the consent of the parties is an agreement evidenced in writing.

Section 107(5) – An agreement alleged by one party and not denied by the other in adjudication, arbitration or court is an agreement in writing for the purposes of the application of the Act subsequently.

Section 107(6) – An agreement recorded by any means is in writing.

Proposal

We are proposing to remove the restriction of the application of the Construction Act to contracts in writing. The effect will be that the Act will apply to construction contracts which are agreed wholly in writing, only partly in writing, entirely orally or varied by oral agreement.

Certain important contractual provisions required by the Act, such as provisions relating to a contractual adjudication scheme, will continue to need to be in writing. Where this is not the case, the relevant provisions of the Scheme will apply. The contract will still be a ‘construction contract’ for the purposes of the Act.

The Scheme

We believe that the various references to ‘agreements’, whether written or oral, between the parties in the Scheme, will be understood to refer to any agreement following the amendments proposed above. We will therefore specify in the Scheme that agreements must be made in writing. We consider the agreement of an adjudicator under Part 1 paragraphs 2 and 5(2) must be made in writing.

The references in the Scheme to written notices and notices in writing are unhelpful and we propose to remove them. Section 115 makes clear that notices under the Construction Act are intended to be in writing, whether or not this is specified explicitly.

Discussion

The practical difficulty of agreeing a full written contract has acted as a barrier to the referral of disputes. Our proposal extends the application of the Construction Act to oral and partly oral construction contracts. Large numbers of construction contracts contain orally agreed terms. Adjudication is strongly supported throughout the industry and increasing access to it is a clear benefit of our proposal.

This proposal is not intended to encourage more oral or partly oral contracts, nor is it likely to do so. There are wider business benefits to contracting on a clearly recorded basis which act as a clear incentive to do so.

The incidence of jurisdictional challenge is reducing the effectiveness of adjudication and increasing its cost. Glasgow Caledonian University's August 2005 report on adjudication found that challenges to the adjudicator's appointment featured in 40% of adjudications. Of these, 3% related specifically to whether the contract was in writing. As a further 7% relate to unspecified challenges to the adjudicator's jurisdiction which are likely to include challenges alleging an oral agreement. Many of these then lead to enforcement proceedings.

The annual reports of the Technology and Construction Court for 2005 and 2006 suggest that on average approximately 100 claims for enforcement of adjudications are submitted each year. The Technology and Construction Solicitors Association has found that, of 154 enforcement cases they considered, 23 (or 15%) related to whether the construction contract was in writing. *Improving payment practices in the construction industry* found that on average this may cost £12,500. The total approximate cost is therefore $100 \times 15\% \times £12,500 = £187,500$.

Based upon Glasgow Caledonian University's reports, we believe it is reasonable to assume that approximately 1,750 adjudications are conducted each year in England and Wales. This is an estimate based on construction output in England and Wales as a proportion of that in the UK and taking an average of 2,000 adjudications per year in the UK based upon the survey. The average cost of enforcement proceedings per adjudication is therefore $187,500 / 1,750 = £107$.

2. Prohibiting agreements that interim or stage payment decisions will be conclusive

Background

Prior to the introduction of adjudication under the Construction Act it was rarely possible to resolve payment disputes via litigation or arbitration during the project. As adjudication is a quick form of dispute resolution, interim or stage payment disputes can now be resolved before the project has come to an end. However, construction contracts often provide that a payment decision will be conclusive of the amount of an interim or stage payment. The effect of such clauses is to prevent the referral of disputes relating to an interim or stage payment decision to adjudication. The decision has already concluded the matter.

The ability of the parties to agree that such decisions are conclusive of the payment amount is reflected at paragraph 20(a) of the Scheme which provides that an adjudicator may not open up, revise or review any decision or certificate if the contract states that the decision or certificate is final and conclusive.

Current legislation

Section 108 of the Construction Act provides the right to refer a dispute under a construction contract to adjudication. The contract must provide a process whereby a party may give notice at any time of his intention to refer a dispute to adjudication.

Section 109 of the Construction Act requires all construction contracts of duration 45 days or more to provide for payment by instalments, stage payments or other periodic payments.

Paragraph 20(a) of Part I of the Schedule to the Scheme provides that an adjudicator may not open up, revise or review any decision by any person if the contract states that the decision or certificate is final and conclusive.

Proposal

We are proposing to provide that –

- An agreement that a decision will be conclusive as to the amount of an interim payment, whether an instalment, stage or other periodic payment, will be ineffective. Decisions as to the amount of a final payment (which are often governed by clauses making them conclusive after a period of time) are excluded.

- The parties may agree that a payment decision is conclusive of the amount of an interim payment after the decision of the amount of the interim payment has been taken and notified to them (an effective agreement).
- A decision as to the amount of an interim payment will include any decision which relates to work performed under the contract to the extent that it affects the amount of the payment.

This proposal reinforces the combined effects of sections 108 and 109 of the Construction Act by providing a right to stage or interim payments which are properly determined in accordance with the contract.

The Scheme

Following the above amendment, parties will no longer be able to agree that interim decisions will be final and conclusive as to the amount of the payment unless that agreement is entered into after the parties have been notified of the amount of the interim payment. We therefore propose to provide that the adjudicator's ability to "open up, revise and review a decision" applies unless the parties have made an effective agreement to the contrary.

Discussion

Following the consultation on *Improving payment practices in the construction industry*, we have concluded that –

- The current incidence of agreements that interim or stage payment decisions should be conclusive is high (responses to the consultation suggested 15% of contracts provide for conclusive decisions that are only of substance to interim payments).
- This can be viewed as a means of avoiding the referral of interim payment disputes to adjudication and is contrary to the intention of the Construction Act.
- The adjudicator's power to open up conclusive interim or stage payment decisions should extend to decisions about the work done in relation to the interim payment.
- Though it can be argued that some stage payments are finally decided at the completion of a stage of work, this is rare as there is often a reappraisal of the valuation of all stages at the completion of the contract.

DTI statistics suggest that 15,000 contracts are of a duration of less than 45 days and that the remaining 85,000 in the industry are therefore subject to the statutory right to interim payments. Interim payments are usually monthly so assuming that each contract provides for a final payment at its completion and an interim payment at the completion of each whole month during the contract, 492,000 interim payments are made each year across the industry. 15% of these payments may not be referred to adjudication leaving 418,200.

The joint DTI / CIC survey³ of adjudicators found that 50% of adjudication disputes relate to interim payments while the remainder relate to final payments or other matters. The survey also found that resolving payment disputes at the interim stage reduced the cost of adjudication by approximately 10%, or £2,000. This means that approximately 875 adjudications in England and Wales relate to interim payments. If adjudication of interim payments was encouraged by increasing the number that may be disputed by a factor of 100 / 85, this would represent an additional 154 interim payment adjudications. Compared to adjudication of the final account, this would result in an approximate reduction in the average cost of £309,000 or £176 per adjudication on average. Any arbitration or litigation cases that were also averted would increase this figure.

The more significant benefit resulting from the prompt payment of the correct sum following the adjudication is more difficult to quantify as the dispute may be decided in favour of either party.

³ Joint DTI/CIC Survey took place between January through to March 2007

3. Introduction of a statutory framework for the costs of adjudication

Background

The Construction Act provides that a party to a construction contract has the right to refer a dispute arising under the contract for adjudication.

One of the disincentives to parties to a contract in referring disputes to adjudication is the financial cost in doing so. Parties can agree in the contract that the 'loser' will pay the costs of the adjudication, or even that, win or lose, the referring party⁴ will bear all the costs. This creates a disincentive to the party so liable for costs to refer disputes to adjudication and can conversely encourage the other party to escalate costs.

Current legislation

Section 108 provides a statutory right to refer disputes to adjudication. It also sets out the basic requirements of the adjudication scheme to be contained in the contract such as the timetable for securing the appointment of the adjudicator

Following a consultation by the Department of the Environment, Transport and the Regions in 2001, DTI has developed proposals for a statutory framework in relation to the costs of the adjudication which:

- ensures that the parties should pay their own legal and other costs thereby providing an incentive to reduce costs unless they agree otherwise after the adjudicator is appointed;
- provides that agreements about payment of costs between the parties are only valid if made in writing after the appointment of the adjudicator; and,
- provides a statutory entitlement for the adjudicator to recover his fees and expenses.

Proposal

We are proposing to include new provisions in the Construction Act so that the following agreements are only valid if made in writing and after the appointment of the adjudicator –

- Agreements that a party should pay the whole or part of the costs of the adjudication (the legal or other costs of the parties and the fees and expenses of the adjudicator).
- Agreements that the adjudicator may make a decision that a party should pay the whole or part of the costs of the adjudication.

⁴ These agreements first arose in the case of Bridgeway Construction -v- Tolent Construction (11 April 2000) and were a particular concern of respondents to Improving adjudication in the construction industry (Department of the Environment, Transport and the Regions 2001) and Improving payment practices in the construction industry (DTI and the Welsh Assembly Government 2005).

Where the parties have made a valid agreement described above, unless the parties have agreed what costs of the adjudication will be recoverable, the adjudicator will be required to award:

- only a reasonable amount in respect of costs reasonably incurred by the parties; and
- such reasonable amount as the adjudicator shall determine by way of fees for work reasonably undertaken and expenses reasonably incurred.

We also intend that, notwithstanding the adjudicator's contractual entitlement to his fees and expenses, the parties shall be jointly and severally liable for the adjudicator's reasonable fees and expenses (the formula above). This "backstop" is intended to ensure the adjudicator can recover his reasonable fees when:

- he decides the dispute; or
- his appointment is brought to an end for reasons other than his default or misconduct.

We have considered whether the Construction Act could include a similar provision requiring the adjudicator to make an allocation of his fees and expenses between the parties. This is not possible if the parties are to be jointly and severally liable for fees. An allocation by the adjudicator appears to be no more than a statement of the proportions in which he will seek to recover them from the parties. It is not binding on him as he is not a party to the dispute.

We will provide that in general the decision of the adjudicator as to the costs of the adjudication is final and binding other than in cases where:

- the parties agree that the adjudicator shall make a decision as to their reasonable legal and other costs and he fails to do so; or
- the adjudicator claims or decides his reasonable fees and expenses under the new provisions.

In these cases we will provide the courts with powers to determine the matter.

The Scheme

Having made full statutory provision for the costs of the adjudication in the Construction Act, we intend to remove all provisions as to the costs of the adjudication from Part 1 of the Schedule to the Scheme for Construction Contracts. These are:

- the provisions entitling the adjudicator to his fees when his appointment is revoked under paragraph 11; and
- the provisions entitling the adjudicator to his fees when he decides the dispute under paragraph 25.

We are also proposing to remove the provisions entitling the adjudicator to payment where he resigns in certain cases where he does not have jurisdiction to decide the dispute. As the Scheme does not apply in these situations, the terms of the adjudicator's appointment determine his payment in this case.

Discussion

We are creating a framework which will provide greater access to the adjudication process for those in the construction industry who would otherwise be reluctant to go through this process because of the costs involved. Our proposal will, to a degree, allow all parties to compete on a 'level playing field'.

We will provide that the parties may not agree before a dispute has arisen and the adjudicator has been appointed, that one party will be liable for all or part of the costs of the adjudication. This provision will remove a disincentive to refer disputes whilst at the same time reducing any incentive to refer frivolous disputes.

In addition, we believe we are encouraging parties to keep costs at a reasonable level by providing that, where the adjudicator is to make a decision as to who shall pay the costs of the adjudication, he shall only award a reasonable amount to reflect costs reasonably incurred. This will also encourage the parties to keep costs at a reasonable level and result in disputes being resolved more promptly.

The parties in dispute will share liability for the adjudicator's fees and expenses. This will ensure the adjudicator can secure payment of his fees and expenses and reduce the possible financial cost to him if he is not paid. This proposal will also ensure that the adjudicator's allocation is impartial because he will not be tempted to allocate his fees to the party better able to pay.

The adjudicator will also not need to ask the parties to sign an 'adjudication agreement' upon his appointment to secure their fees and expenses.

The joint DTI / CIC survey of adjudicators suggested that the parties' combined legal and other costs in an adjudication are approximately £15,000. The same survey found that the adjudicator's fees and expenses are approximately £5,000 on average. The total costs of the adjudication are therefore approximately £20,000. Statistics from the CIC in 2001 suggested that the incidence of agreements that the referring party should pay all of the costs of the adjudication arise in 3% of adjudications. Results from the DTI / CIC survey were unclear and the extent of the problem is considered as part of this consultation. If these clauses arise in 3% of the 1,750 adjudications each year and, in each one, on average half of the costs are unfairly allocated at a cost of £525,000 this will cost £300 per adjudication on average.

Chapter 2 – Payment framework

Overall Background

To help achieve its objective of ensuring prompt cash flow and allowing the swift resolution of disputes by way of adjudication the Construction Act sets out a payment framework.

- **Section 109** introduces a right to instalment, stage or periodic payments
- **Section 109(2)** provides that the parties are free to agree the amounts of the payments and the intervals and circumstances in which they become due
- **Section 110(1)** requires the contract to have an adequate mechanism for determining what will become due and when
- **Section 110(2)** provides that the payer gives the payee early communication of what will be paid
- **Section 111** provides that the payer may not withhold money unless he has effectively communicated this to the payee.
- **Section 112** provides that a payee may suspend performance when the amount due is not paid by the final date for payment
- **Section 113** prohibits so called “pay when paid” clauses

This payment framework creates the means of crystallising the amount to be paid on or before the final date for payment for each instalment, stage or periodic payment. It does this by introducing the concepts of sum due and due date together with a requirement to issue notices during the payment period to communicate the basis on which the amount paid or proposed to be paid has been calculated.

- The due date is the contractually agreed milestone which starts the payment period.
- The payment period is the time between the due date and the final date for payment. The length of this period is a matter for contract.
- The sum due is a notional amount determined by the contract which begins the process of crystallising the amount payable on the final date for payment.
- The final amount for payment is the sum due minus deductions – some of which are required to be set out in section 111 withholding notices.

The problems associated with the operation of the payment framework have been considered at each stage of the review of the Construction Act. The proposals in this chapter have resulted from consideration with our sounding board. We have revisited the conclusions of *Improving payment practices in the construction industry* and the proposals made in the

January 2006 consultation analysis, particularly in respect of the potential roles of the payer and payee in 'certifying payments'. We have tried to identify the most appropriate balance between effective regulation and reducing the regulatory burden, particularly in respect of the notice requirements sections 110(2) and 111.

1. Prevention of unnecessary duplication of payment notices

Background

Section 110(2) requires the payer to issue a payment notice setting out the payments made or proposed to be made not later than five days after the date on which a payment becomes due. However, under most contracts with certificates the information in the payment notice only duplicates the information already contained in the certificate. For those contracts, this represents a needless duplication.

Current legislation

Section 110(2) requires every construction contract to provide for the payer to give notice not later than five days after the date on which a payment becomes due from him under the contract, or would have become due if

- (a) the other party had carried out his obligations under the contract, and
- (b) no set-off or abatement was permitted by reference to any sum claimed to be due under one or more other contracts,

specifying the amount (if any) of the payment made or proposed to be made, and the basis on which that amount was calculated.

Proposal

Intended purpose

To prevent unnecessary duplication by allowing a notice or certificate from a third party to act as section 110(2) payment notice.

The Construction Act

This proposal relates primarily to the drafting of section 110(2) of the Act. We consider that, as well as the party from whom payment is due, certain other people should be able to issue a payment notice complying with section 110(2). We propose that, where the contract provides, the Act should allow the notice to be issued by:

- a person identified in the contract; or
- a person who has been identified in a notice to the payee.

The Scheme

We propose to amend paragraph 9 of Part II of the Scheme to make provision for a payment notice in accordance with the new provisions in section 110(2) of the Act. Under the Scheme a payment notice cannot be issued by a named individual so we propose that it should be issued either by:

- the person from whom payment is due; or,
- a person who has been identified in a notice to the payee.

Discussion

The current framework creates notice requirements which duplicate certification procedures. Under approximately 60% of main contracts a certificate is issued by an architect, engineer or surveyor to determine the sum due. Shortly afterwards the payer must issue a payment notice stating the amount to be paid. The payer is usually happy to pay the sum due as certified and the information in the notice only duplicates that in the certificate. There is a significant financial cost associated with the administrative inconvenience of complying with both requirements. DTI statistics suggest that 396,000 main contract payments are made each year. Responses to Improving payment practices in the construction industry suggest that the cost of issuing a payment notice is approximately £25 per payment. Overall this gives us an estimated reduction of $396,000 \times 60\% \times £25 = \text{£}5.94 \text{ million per year}$.

2. Clarification of the requirement that a section 110(2) payment notice should be served

Background

Section 110(2) requires a payment notice to be served in certain circumstances. The simplest of these is where a payment is due. The other is where the payment **would have been due** had a combination of circumstances arisen. We do not consider that the drafting of these provisions is ideal: specifically, it is not clear that the obligation to issue a payment notice continues even where no payment is due because of abatement or set-off under the contract in issue.

Current legislation

Section 110(2) requires every construction contract to provide for the payer to give notice not later than five days after the date on which a payment becomes due from him under the contract, or would have become due if

- (a) the other party had carried out his obligations under the contract, and
- (b) no set-off or abatement was permitted by reference to any sum claimed to be due under one or more other contracts,

specifying the amount (if any) of the payment made or proposed to be made, and the basis on which that amount was calculated.

Proposal

Intended purpose

To make clear that a payment notice is always required if a payment would have become due under the contract. That will be the case even where there is no obligation to make any payment because the work has not been carried out or there has been set-off under the contract, or one or more other contracts, or abatement under the contract.

The Construction Act

We are proposing to amend section 110(2) so that a payment notice will be required where a payment would have been due if:

- the party performing work under the contract had carried out his obligations under the contract;
- no set-off was permitted by reference to any sum claimed under the contract or one or more other contracts; and,
- no abatement was permitted in respect of the work.

The Scheme

We will amend the payment notice provision in Part II paragraph 9 of the Scheme to reflect the amended requirements in the Act.

Discussion

The current drafting of section 110(2) may lead the payer to mistakenly conclude that he need not issue a payment notice because of certain deductions from the sum that would otherwise have been due. Payment notices are an important tool in ensuring early communication of payments made or proposed to be made. Such notices are therefore important even where no payment is proposed because the work has not been carried out, or there are set-offs or abatements that mean the payer is not obliged to pay.

3. Clarity of the content of payment and withholding notices

Background

The Construction Act introduced the requirement that the payer should serve section 110(2) payment and section 111 withholding notices to the payee. There is confusion in the industry about how they relate to each other, what each should contain and how they create a sum due. This lack of clarity can lead to the needless issue of two separate notices when a single payment notice would have sufficed.

Clearly, measures to improve the clarity of notice content will help address some of the issues relating to a sum becoming due which is considered in section 4 of this chapter.

Current legislation

Section 110(2) requires every construction contract to provide for the payer to give notice not later than five days after the date on which a payment becomes due from him under the contract, or would have become due if

- (a) the other party had carried out his obligations under the contract, and
- (b) no set-off or abatement was permitted by reference to any sum claimed to be due under one or more other contracts,

specifying the amount (if any) of the payment made or proposed to be made, and the basis on which that amount was calculated.

Section 111(1) requires a party withholding payment after the final date for payment of a *sum due* to give an *effective withholding notice*.

It also provides that a section 110(2) notice may be an effective withholding notice if it complies with section 111.

Section 111(2) describes an effective withholding notice. It must specify

- (a) the amount proposed to be withheld and the ground for withholding payment, or
- (b) if there is more than one ground, each ground and the amount attributable to it,

and must be given not later than the *prescribed period* before the final date for payment.

Section 111(3) allows the parties to agree the prescribed period and provides that in the absence of agreement the period is that provided in the Scheme.

Proposal

Intended purpose

- To introduce clarity as to the content of the payment and withholding notice framework
- To prevent unnecessary duplication by making clear provision on how a section 110(2) notice can act as a withholding notice; and
- To align the information required in section 110(2) payment notices and section 111 withholding notices.

The Construction Act

We are proposing that the payer must set out in the payment notice the amount (if any) that he has paid or proposes to pay.

Where this is different from the amount that would have been paid had:

- the payee carried out his obligations under the contract;
- no set-off was permitted by reference to any sum claimed under the contract or one or more other contracts; and,
- no abatement was permitted in respect of the work,

we propose that payer will have to set out the grounds for paying less than the amount calculated in accordance with the above formula. Where there is more than one ground for making deductions from that amount, the payer will be required to set out each ground and the amount attributable.

Further, we are proposing to require that all withholding notices should be in the same format as a section 110(2) notice with the effect that the withholding notice becomes a revision of the payment notice.

Once the 'prescribed period' under section 111(3) has passed, the payer cannot revise the amount in the notice any further.

We propose to make clear that the withholding requirement is in respect of any amount (i.e. including abatement) and not just withholding "of a sum due" as at present (which is thought by many only to relate to set-offs).

The Scheme

We will make changes to align the Scheme with the above in respect of payment notices.

Discussion

Our proposal creates a clear connection between the information in the section 110(2) notice and that required to withhold payment in accordance with section 111. This will remove unnecessary duplication in the system as we understand some payers routinely submit both a payment notice and a withholding notice at present where only one is necessary.

Our proposal sets out a framework where a withholding notice should take the form of a revised payment notice. This single format creates clarity and simplicity, though in places additional information is required.

The proposal that the withholding notice would be required to state the amount of the payment made or proposed to be made was supported in *Improving payment practices in the construction industry* in 2005. Though we had initially rejected that proposal following the consultation, further consideration has led us to conclude that it would allow the payment and withholding notice requirements to work more effectively and economically.

Administrative cost

It is arguable that this proposal will increase the number of section 111 withholding notices that must be issued under contracts without certificates. It is possible to estimate the cost to the construction industry of this change using DTI's estimate that 356,400 payments are made each year under contracts without certificates (40% of main contract payments and an additional 50% as an estimate for the number of payments made under sub-contracts).

We are seeking responses from consultees on the proportion of payments that are subject to abatement after the payment notice deadline but, if it is one monthly payment every two and a half years, and the cost of a withholding notice is £25, we estimate that the additional inconvenience will cost the construction industry in England and Wales $356,400 \times £25 / 30$ = **£297,000 per year**.

4. Clarity of the sum due

Background

In the Construction Act the sum due is the cornerstone on which the rest of the payment framework is built.

The concept of what constitutes the sum due is clear where the contract provides for certification of work by a third party (such as an architect). In these cases the courts have upheld the position that sum due is the amount in the certificate.

However, in contracts without certificates the position is less clear and the current payment framework can fail to create a clear understanding between the parties as to what is the sum due. As a result the Act can fail to effectively crystallise the amount to be paid on or before the final date for payment or allow access to the right of suspension.

Proposal

The Construction Act

We are proposing that where the payer has issued a payment notice as described in section 3 of this Chapter this amount becomes the sum due, which can then be subject to withholding. Non-payment of the remainder will provide the payee with the right to suspend performance.

We would then provide that –

- Where the payment notice is not issued, the sum due is determined by a new fallback provision. The sum due would then be the amount in a claim by the payee issued before the final date for payment.
- Where that claim determines the sum due but is issued after the due date, the payment period would then run from the date of the claim to allow the payer time to issue a withholding notice.

We would also provide that, like the current provision in section 111(4) for amounts to be withheld, the amounts to be paid under a payment notice could be referred to adjudication and the payment delayed until a week after the date of the adjudicator's decision.

The Scheme

We are proposing that the fall-back provision whereby the sum due is determined by a claim by the payee should take effect as a statutory fall-back, rather than a requirement that the contract should provide this fall-back. As such, no corresponding provision is necessary in the Scheme.

Discussion

Section 110(2) requires the contract to provide for the payer to notify the payee of “the amount (if any) of the payment made or proposed to be made”. There are two practical problems with this.

- It is not clear how the amount specified in the notice relates to the sum due. The sum due is not then clear for the purposes of sections 111 and 112.
- Failure to issue the notice may be no more than a minor breach of contract. This is because nothing in section 110(2) compels the payer to issue it. *Improving payment practices in the construction industry* found that the notice is only issued for about 40% of payments.

Where these problems arise, their effect on sections 111 and 112 of the Construction Act raises the following issues.

Section 111 enables a payer to withhold payment from a sum due where he has issued a withholding notice. In the absence of a withholding notice the payer must pay the whole sum due. However, the lack of transparency about what constitutes the sum due (whether or not he has received a section 110(2) payment notice) can leave the payee with less payment than expected. This can result in costly legal proceedings to determine the ‘sum due’. It can often be argued that no notice is needed as the abatements were never due. Generally, set-offs should be notified, though this may differ under certain contracts. In any respect, the majority of contractors cannot distinguish one form of deduction from the other.

Section 112 provides a right to suspend performance where the payer fails to pay the sum due (subject to any withholding under section 111). However the lack of transparency about what constitutes the sum due acts as an effective barrier to the exercise of this right.

We therefore intend to introduce much greater transparency about the sum due by providing a statutory definition.

5. Prohibiting the use of pay-when-certified clauses

Background

As part of the proposal to create a clear understanding of the sum due under a construction contract we have concluded there may be value in restricting the use of pay-when-certified clauses. This ensures that there is clarity about [when](#) payments become due as well as what the sum due is.

Current legislation

- **Section 110(1)** of the Construction Act provides that “every construction contract should provide an adequate mechanism for determining what payments become due under the contract, and when”. This provision allows payment to be triggered by the timing of a decision which is conditional on work under a separate contract.
- **Section 113** of the Construction Act states that “A provision making payment under a construction contract conditional on the payer receiving payment from a third person is ineffective”. This prohibition of pay when paid clauses also does not appear to affect a clause making the timing of payment conditional on [a decision](#) about payment from a third person.

Proposal

The Construction Act

As part of a new payment framework, we are proposing to ensure that a certificate covering work under one contract cannot act as a mechanism to determine the timing of payment for work done under another contract. In effect we propose to prohibit pay-when-certified clauses.

The Scheme

No amendment to the Scheme is necessary

Discussion

Respondents to *Improving payment practices in the construction industry* suggested that pay-when-certified clauses were a way for the main contractor to shift the burden of non-payment to the sub-contractor. The sub-contractor has no way of knowing whether a main contract certificate has been issued, or its contents, or whether the payer has grounds under the pay-when-certified clause to withhold payment.

Although prohibiting pay-when-certified clauses may have the result that the main contractor pays the sub-contractor before he himself is paid, it is in keeping with the purpose of the Act for funds to be distributed through the construction supply chain promptly.

Our proposal is seeking to ensure that, provided a sub-contractor has completed the work he has been engaged to do, once he issues his invoice the payer must pay regardless of whether a certificate has been issued under the main contract.

This will ensure that money flows through the supply chain thereby reducing the need for companies to service loans/debts. The benefit to the whole supply chain is that firms can better manage their cash flow. We would also expect there to be fewer disputes.

In assessing the impact of this proposal, we are only proposing to consider its effect on standard forms of sub-contract. We understand that traditional civil engineering sub-contracts continue to include pay-when-certified clauses. DTI statistics suggest that 11,400 payments are made each year under civil engineering sub-contracts. As these will no longer become due under a pay-when-certified clause, the terms of the Scheme will apply and the payment will become due following the expiry of the relevant period or upon the issue of a claim by the payee, whichever is the later. The payer will then have to issue a payment or withholding notice. Assuming a main contract certificate has not been issued, this will require additional administration by the payer. Assuming a cost of £25 the total cost will be **£285,000**.

Overall benefits of the revised payment framework

We believe the revised framework will:

- improve communication between the parties;
- enable cash to flow through the supply-chain and improve liquidity and reduce costs of servicing debt; and
- enable the parties to address problems that give grounds for withholding payment.

The reduced burden of the revised payment framework is approximately £5.4million.

Simplification of payment notices	£5,940,000
Clarity as to the sum due	- £ 297,000
Pay when certified	- £ 285,000
TOTAL	£5,358,000

The broader benefit of the new framework is the creation of clear entitlements to payment which may be reviewed at adjudication in an arrangement that is comparable to interim certification under many forms of construction contract. This will enable disputes to be resolved at an early stage in any given payment period. We believe this will reduce financial costs for both the payer and the payee prioritising the need for payment to crystallise and change hands at an early stage rather than being delayed by the determination of the amount legally payable irrespective of the delay. This is of considerable benefit to the industry and its customers.

Quantifying the saving to the construction industry and its clients in terms of reduced cost and improved productivity and efficiency is difficult. However, OGC recently commissioned research in support of the Fair Payment Charter which indicated that improvements to the payment framework to ensure contracts create clear and timely entitlements to interim payment are estimated to save 1% – 1.5% on the average project. If this were reflected across construction in England and Wales, it would represent £1 – 1.5 billion.

To identify overall the savings that result specifically from our proposals we have considered the comparison between the operation of contracts with certificates and of contracts without certificates. In future, the section 110(2) payment notice will act like a certificate in creating an entitlement to payment subject to withholding under section 111 and final determination by adjudication, arbitration or litigation. In the absence of a payment notice, a claim by the payee will determine the sum due on the same basis. A similar system also operated on the Joint Contracts Tribunal “With Contractor’s Design” contract until its revision in 2005. Statutory support for this approach would be likely to ensure its effective operation.

Chapter 3 – Improving the right to suspend performance

Background

The Construction Act provides a statutory right for the payee to suspend performance under the contract. This right:

- is a powerful sanction in cases of non-payment, and
- allows the payee to reduce his expenditure on the project during a period when he is not being paid.

However, there are a number of disincentives to the exercise of this right which centre on the costs of suspending performance.

Current legislation

- Section 112(1) gives a statutory right to the payee to suspend performance of obligation to the payer in cases of non-payment of a sum due (less any amounts properly withheld).
- Section 112(2) provides that the right can only be exercised if the suspending party has given the payer in default seven days notice of his intention to suspend work stating the reasons why work will be suspended.
- Section 112(3) provides that the right to suspend work ends when the outstanding amount is paid in full.
- Section 112(4) provides that there should be a readjustment to the contract to compensate for the time lost during a period of suspension.

Proposal

We intend to make the existing right to suspend performance a more effective remedy by reducing the burden on the party who exercises this right. We will:

- make clear that a party need not suspend all of his obligations to the party in default when exercising the statutory right;
- provide a statutory right for the suspending party to be compensated for reasonable losses caused by the suspension; and
- provide an extension of time for any delay caused by the exercise of the right to suspend.

Discussion

Our proposals are intended to make the right of suspension more accessible and effective. The measures are not intended to alter radically the process and should decrease the costs of suspension to the suspending party. Without access to the statutory right of suspension, the payee cannot secure prompt payment or take steps to reduce his expenditure when he is not paid.

The following disincentives upon the suspending party result from the current legislative framework –

- *The costs of suspending and remobilising performance under a construction contract* – These are the inherent costs involved in exercising the right of suspension and then remobilising when payment is made. These costs, which may include damaged materials while clearing site, storage charges, additional management costs and the cost of retaining sub-contract labour and hired plant and equipment all fall to the suspending party (the payee). The possibility of incurring additional costs for remobilisation when the payer later makes the outstanding payment is also a burden. The current legislation requires the payee to remobilise immediately upon payment which can impose additional cost.
- *The inconvenience and cost of remobilising immediately upon payment of the outstanding debt* – Currently, the Construction Act makes no allowance for any delay for the suspending party to remobilise. The suspending party is required to be prepared to remobilise immediately when payment is made as the contract may also impose a sanction. Given the uncertainty about whether the payment will be made, and if so when, and to reduce the costs of suspension, the payer may have transferred labour and equipment to a different project.
- *The inconvenience and cost of having to suspend all obligations under the contract* – We believe that the right of suspension can be exercised in respect of suspension of any or all of the payee's obligations under the contract. However this view is not shared with the whole construction industry and there is support for some clarification.

In *Improving payment practices in the construction industry* we asked how frequently the right to suspend performance was exercised and how frequently it was believed it would be exercised following our proposed amendments. While the majority of respondents thought it was exercised in fewer than one in 100 cases of defaulted payment at present, almost half thought that this would increase to between one in 100 and one in 10 cases of defaulted payment in the future.

Though there might be a modest increase in the use of the statutory right to suspend performance following the amendments proposed above, we also intend that improving access to the right should ensure that payment is made on time more often in future. We are considering the extent of any improvement in payment as a result of these proposals as part of this consultation.

Chapter 4 – Other issues which we are considering as part of this consultation

1. Devolution

Background

This is a joint consultation between the DTI and Welsh Assembly Government. It considers amendments to Part II of the Housing Grants Construction and Regeneration Act 1996, which would be taken through the UK Parliament by the UK Government and would affect both England and Wales.

This consultation also covers amendments to the Scheme for Construction Contracts (England and Wales) Regulations 1998. In so far as they affect England these would be taken through the UK Parliament by the UK Government immediately after the primary legislative amendments have been passed. In so far as they affect Wales, the amendments to the Scheme will need to be taken through the Welsh Assembly separately by the Welsh Assembly Government.

The Construction Act also applies in Scotland. Policy responsibility for the Act in Scotland and the Scheme for Construction Contracts (Scotland) Regulations 1998 is a matter for the Scottish Executive. Any amendments affecting Scotland would be a matter for the Scottish Parliament. DTI officials are in regular contact with officials in the Scottish Executive. We understand that the Scottish Executive is developing commensurate proposals to those in this paper.

Work with the devolved administrations to maintain cross border uniformity

It is a long established policy that, though responsibility for this legislation has been transferred to the devolved administrations, where possible the administrations will work together to ensure that divergence in effect should be minimised. It is accepted that certain legal differences between Scottish and English Law may necessitate modest differences in approach (as is already the case), but by working with the Scottish Executive in respect of policy development we would hope to keep these to a minimum.

The Scottish Executive's consultation on *Improving adjudication in the construction industry* in 2003 asked respondents for their views on maintaining cross border uniformity so far as is possible and found general support. We are doing the same in this consultation (see the consultation response form).

2. Correction of errors

Background

Maintaining cross border uniformity on the Construction Act could raise several issues. Our intention is that if respondents to this consultation support a preference for cross border uniformity, so far as is possible we will continue to seek to agree proposals with the Scottish Executive to bring this about.

One issue which has already arisen, and where we are seeking the views of respondents on cross-border uniformity, is the suggestion that emerged in 2004 from the Scottish Executive's consultation on Improving adjudication in the construction industry for a "slip rule".

Scottish Executive proposal

The Scottish Executive's report of its consultation on *Improving adjudication in the construction industry*⁵ suggested that a "slip rule" should:

"...give adjudicators powers to correct their decisions so as to remove any clerical, or arithmetic, mistake or error that has arisen from an accidental slip or omission; and they should be permitted to do this at the request of any party to the adjudication, and where the adjudicator becomes aware of such an error. It is also proposed that adjudicators should be empowered to correct any other aspects of their decisions where the parties are in agreement that they should do so.

"Any corrections of clerical or arithmetic errors are likely to be relatively straightforward, and so the timescale for notifying the adjudicator, and for making corrections, need not be particularly lengthy, bearing in mind the need to achieve relatively quick resolution of disputes. It is proposed, therefore, to amend the Scheme to provide that adjudicators may make corrections as soon as possible and by not later than seven calendar days after the date of issue of their decisions or such longer period as the parties may agree. This should allow sufficient time for corrections to be made without unduly delaying the process.

"Consideration has been given to whether there is a need to set a time limit for parties to request an error to be corrected. It is felt that by setting a time limit on the period allowed for correcting a decision, and giving adjudicators discretion on whether or not they make a correction, there should not be a need to set a time limit within which the error must be brought to the adjudicator's attention."

⁵ See www.scotland.gov.uk/Publications/2004/05/19360/37122 (chapter 5)

Further background on the Scottish Executive's proposal can be found in the original consultation paper⁶. We understand that the Scottish Executive is continuing to develop this proposal.

Consultation

We are seeking the views of respondents to this consultation on whether, in order to have a uniform effect across in England, Scotland and Wales, the DTI and Welsh Assembly Government should work with the Scottish Executive to further develop proposals for a slip rule. In particular we are seeking the views of respondents on whether the slip rule should provide the adjudicator with:

- power to correct a clerical or arithmetic error or any other matter that the parties may agree
- for one week after the adjudicator's decision or such longer period as the parties may agree.

In England and Wales, it has not been necessary to introduce a slip rule as the courts have implied such a rule by reference to the Arbitration Act 1996. However if introduced in England and Wales, legislation would remove the courts' current discretion as to the time limits and applicability of a slip rule.

⁶ See www.scotland.gov.uk/consultations/industry/iaci-00.asp (chapter 3.5)

3. **The judgement of the House of Lords in Melville Dundas -v- George Wimpey**

Background

This judgement relates to a Scottish case. However, it concerns the interpretation of the Construction Act as it applies in England and Wales (and in similar legislation in Northern Ireland) as well as Scotland. It is likely to be followed across the UK. We are seeking the views of consultees on:

- whether the judgement raises an issue which must be addressed via a legislative amendment; and,
- what options there are for addressing those issues.

The case

In the case, Wimpey employed Dundas to construct a housing development. On 2 May 2003, Dundas applied for an interim payment. There was no dispute that this payment was due. The final date for payment was 16 May (14 days after Dundas' application). On 30 May 2003, Wimpey terminated the contract due to the appointment of an administrative receiver to Dundas. The contract provided that where Wimpey terminated the contract it was not obliged to pay any payment due which accrued less than 28 days before the earliest date that Wimpey could have first given notice to terminate the contract (22 May).

Dundas sought to enforce the payment in the Outer House of the Court of Session in Scotland claiming that the payment ought to have been made on or before the final date for payment, notwithstanding the termination of the contract. No withholding notice had been issued in accordance with section 111 of the Construction Act before the 11 May contractual deadline. Lord Clarke refused to enforce the payment, stating that the payment had not been withheld but that the final date for payment had been delayed while a final payment following termination was calculated. This was overruled by the Inner House of the Court of Session (Appeal Court in Scotland). On 25 April 2007, by a majority of 3 to 2, the House of Lords restored Lord Clarke's original judgement, though for different reasons.

The judgement

The reasoning of the prevailing judgements in the House of Lords can be summarised as follows –

- The Construction Act is intended to balance the parties' freedom of contract with the need for clarity as to amounts of payments under the contract and any amounts to be withheld. This was intended to balance the interests of the payer and the payee.
- Section 111 should apply to interim payments where these become due by virtue of the statutory right to interim of stage payments in section 109 of the Act. So long as the contract is in operation, a notice would be required for these to be withheld via set-off as a result of a cross claim.
- It was not clear that section 111 applied to withholding under the standard determination clause in the contract because –
 - The determination clause was already drafted in a standard contract so as to balance the interests of the payer and payee.
 - It allowed the payment to be withheld in cases of administration in the same way as would apply under the legislative framework for cases of bankruptcy and liquidation.
 - After the payment was withheld, a final payment would be determined taking into consideration all of the parties respective entitlements. The effect was that the interim payment that had been due was no longer due, and instead a final payment would become due.
- In the absence of clear provision in the Act, the Inner House should not have insisted on the payment being made, but should have found that the determination clause applied.
- The two dissenting Law Lords found that the only way to systematically apply the withholding notice requirement in the Act was to find, as the Inner House did, that, in the absence of a withholding notice, the determination clause did not apply. The Act did not provide an exception to the application of section 111.

Issues raised

We consider that the judgement raises two areas of uncertainty:

- whether section 111 applies in cases where the contract is determined, or only where it is determined in cases of insolvency; and
- whether section 111 applies to other grounds for withholding in respect of final payments.

Policy

From a policy perspective, we consider that –

- **section 111 should not apply in cases of insolvency** – Currently the courts will not enforce the decision of the adjudicator in accordance with section 108 of the Construction Act in cases where the payee is insolvent. The House of Lords considered that the application of section 111 was comparable.
- **section 111 should apply in all other cases** – We consider that section 111 should apply to all other grounds for withholding in respect of all payments (i.e. final payments as well as “payments by instalments, stage or other periodic payments” which become due in accordance with section 109 of the Construction Act) while a construction contract is in operation. It appears clear to us that this was the original intention.

The consultation response form asks respondents whether:

- the House of Lords judgement is likely to be followed by the lower courts so as to have the effect that we consider should apply;
- the Act should expressly provide an exception to section 111 in cases where the payee is insolvent (section 113 already provides an example of an exception for insolvency), or leave this exception to be decided by the courts; and whether
- the Act should be amended to make clear that section 111 applies to all other grounds for withholding in respect of all payments.

Partial Regulatory Impact Assessment

Proposals to amend Part II of the Housing Grants, Construction and Regeneration Act 1996 (the Construction Act) and the Scheme for Construction Contracts (England and Wales) Regulations 1998 (the Scheme)

1. Objective

Disputes under construction contracts can jeopardise the effective delivery of projects on time and within budget. They can also threaten the viability of individual businesses and can undermine the longer-term health of the construction industry. The proposals being considered in this RIA seek to improve the statutory framework set out under the Construction Act to reduce the incidence and impact of these disputes.

We are seeking to introduce a better, more focused and effective regulatory framework by:

- improving the transparency and clarity in the exchange of information relating to payments to enable the parties to construction contracts to better manage cash flow; and
- encouraging the parties to resolve disputes by adjudication, where it is appropriate, rather than resorting to more costly and time consuming solutions such as litigation.

The proposals are proportionate amendments to the existing framework which has, in large part, worked well – rather than wholesale reform.

2. Background

The Chancellor announced in the 2004 Budget Report that:

“Following concerns raised by the construction industry about unreasonable delays in payment, the government will review the adjudication and payment provisions of the Housing Grants Construction and Regeneration Act in order to identify what improvement can be made.”

In April 2004, the then Construction Minister, Nigel Griffiths MP appointed Sir Michael Latham to undertake the first stage of the review. The purpose of this first stage was to identify the extent, for all sectors of the industry, to which the Act:

- Was working well;
- Needed improvement; and
- What any potential impacts on other parties or processes might be.

Sir Michael’s report to Nigel Griffiths (September 2004) concluded that the industry had come a long way since the Construction Act was introduced in 1996 and that it was generally working well. However, the report identified some areas where further progress was desirable. The DTI and Welsh Assembly Government’s March 2005 Consultation exercise, *Improving payment practices in the construction industry*, explored some of these in more detail.

Over the course of this review, the Government has considered a wide range of proposals to change the operation of the adjudication and payment provisions in the Construction Act. The proposals in *Improving payment practices in the construction industry – 2nd consultation* mark the latest stage of that review. We have identified the changes we consider can be made to improve the operation of the Act and have set these out in this document (see paragraph 4 below).

Rationale for Government intervention

Sir John Egan, Chair of the Construction Task Force said in the Foreword to *Rethinking Construction* (1998):

“A successful construction industry is essential to us all. We all benefit from high quality housing, hospitals or transport infrastructure that is constructed efficiently. At its best the UK construction industry displays excellence. But, there is no doubt that substantial improvements in quality and efficiency are possible. Indeed, they are vital if the industry is to satisfy all its customers and reap the benefits of becoming a world leader”

Disputes under construction contracts can pose a major threat to the effective delivery of projects on time and on budget. At the broader industry level, the culture evidenced by such disputes can only undermine the industry's ability to achieve the performance improvements set out in *Rethinking Construction* (1998) and *Accelerating Change* (2002).

As Sir Michael Latham's report in 2004 confirmed, the Construction Act has been generally welcomed since it came into force on 1 May 1998. The adjudication process in particular appears to have reduced the number of disputes reaching the courts. However, payment practices in the construction industry continue to cause concern. Problems of disputed, late and non-payment continue to be commonplace.

3. Consultation

The development of the proposed changes to the current legislation has involved extensive formal and informal consultation with the construction industry, its clients, other stakeholders and Government.

Within Government

We have had discussions with:

- The Cabinet Office
- Office of Government Commerce
- HM Treasury
- The Department for Communities and Local Government
- Department for Constitutional Affairs; and
- Devolved Administrations

With industry

Consultation with the industry has included:

- The review undertaken by Sir Michael Latham in 2004;
- The first consultation *Improving payment practices in the construction industry* in 2005;
- *The Analysis of Improving payment practices in the construction industry* 2006;
- Industry Stakeholder events organised by the DTI Construction Sector Unit in June 2005 and February 2006;
- Industry Stakeholder events organised by the umbrella bodies during the 2005 consultation period; and
- A pre-consultation exercise on adjudication in autumn 2006

DTI also established a sounding board. Sounding board members did not represent specific sectors of the industry but were asked to assist in view of their personal knowledge, experience and access to industry networks. The sounding board has been invaluable in assisting with the preparation of the proposals. Its members were Richard Bayfield, Chris Dancaster, Richard Haryott, Sir Michael Latham, HH Humphrey Lloyd QC and Peter Rogers CBE.

4. Options

Among the alternative options considered was to maintain the legislation as it stands and take forward a voluntary process of improving construction contract and payment practices through guidance.

Government and all parts of the industry have a good track record on working together to improve adjudication. An example of this has been the work of the Construction Umbrella Bodies Adjudication Task Group (CUBATG) in preparing guidance in response to a number of issues and concerns raised during a previous review of the operation of the adjudication provisions of the Construction Act. This guidance is available from the Construction Industry Council Website (<http://www.cic.org.uk/services/adjudication.html>)

We have sought to maintain and build this existing positive relationship with CUBATG in developing our proposals to amend legislation on adjudication and to develop suggestions for areas where further guidance will be helpful.

Throughout the process of this review a number of issues have been raised where it has been decided that 'doing nothing' is the best option. The reasons for taking this approach in those cases have been set out in the public information which accompanies this Review. The key documents are:-

- Nigel Griffiths' letter of 21 October 2004 to Sir Michael Latham
- *Improving payment practices in the construction industry*
 - March 2005 Consultation Document
 - January 2006 Analysis of Consultation Responses
 - Annex A of this Consultation

These are all available on the construction pages of DTI's website

(<http://www.dti.gov.uk/sectors/construction/constructionact/page13956.html>)

A. Targeted regulation

In developing the payment and adjudication proposals we have chosen to go down the 'targeted regulation' route i.e. to intervene where it is clear that the legislation is not meeting the original objectives effectively. We are seeking to 'fine tune' rather than re-invent the existing statutory framework.

Through this approach we have identified a package of legislative measures to address weaknesses and improve the clarity of operation and effectiveness of the existing legislation. Many of these measures are technical and have low regulatory impact. They are outlined below.

Proposals

Prompt and fair payment practice throughout construction supply chains will better enable the industry to adopt integrated team working as the norm.

The amendments to the Construction Act will:

- improve the transparency and clarity in the exchange of information relating to payments to enable the better management of cash flow;
- encourage the parties to resolve disputes by adjudication, where it is appropriate, rather than by resorting to more costly and time consuming solutions such as litigation; and
- improve the right to suspend performance under the contract.

This will be done by:

On adjudication

- improving access to the right to refer disputes for adjudication by:
 - applying the legislation to oral and partly oral contracts
 - preventing the use of agreements that interim payment decisions will be conclusive to avoid adjudication on interim payment disputes
- ensuring the costs involved in the process are fairly allocated

On payment

- preventing unnecessary duplication of payment notices
- clarifying the requirement to serve a section 110(2) payment notice
- clarifying the content of a notice
- ensuring the payment framework creates a clear interim entitlement to payment
- prohibiting the use of pay when certified clauses

On suspension

- improving the statutory right to suspend performance by allowing the suspending party to claim the costs and delay that result.

This is not wholesale reform. These proposals are intended to be light touch and proportionate amendments to the existing framework to address specific issues that have arisen during the nine years the Construction Act has been in operation. Guidance remains the preferred route to improve operation of construction contracts and we have only considered further legislative intervention where we believe it is absolutely necessary.

B. Extensive regulatory intervention

The other option which is not being pursued is that of '**extensive regulatory intervention**'. As the review of the Construction Act has progressed, some proposals have been suggested which, in our view, would undermine the compromises that were reached in 1996 or would fundamentally alter the existing statutory framework. Throughout the review process, we have been mindful of the finely balanced compromise that was struck by the original legislation. Our guiding premise therefore has been only to intervene where it has been considered that the legislation has shown to not have delivered its original objective. We have only intervened in ways which do not undermine the existing structure of the legislation. Such proposals that we do make are targeted interventions to "fine tune" the existing statutory framework.

Following a more regulatory route would be to change fundamentally the Construction Act and the contracts it regulates. At the very least this would impose considerable transitional burdens on the industry and its customers. For instance the large number of standard forms of contract (as an example the Joint Contracts Tribunal has some 20 contracts) would need to be revised extensively as the transition was made from one statutory framework to another with the resultant additional costs and disruption that entails.

6. Costs and benefits

The proposals we are seeking to introduce to amend the Construction Act will:

- improve access to the adjudication system by applying the legislation to oral and partly oral contracts and ensuring the costs involved in the process are allocated fairly;
- improve the operation of the payment framework in the legislation by removing the duplication between statutory payment notices and contractual payment certificates; and,
- ensure the payment framework operates effectively to create a clear interim entitlement to payment which can be finally determined through arbitration or adjudication if necessary.

The costs and benefits of each of these proposals are summarised in the following table.

Proposals	Benefits	Costs	Net Benefit
Prevention of unnecessary duplication of payment notices	A significant reduction in the number of payment notices that need to be issued by the payer. This reduction in the requirement for Section 110(2) notices will save the industry approximately £5.9million .		<ul style="list-style-type: none"> ■ Our proposals create a clear connection between the information in the section 110(2) notices and that required to withhold payment in accordance with section 111. This will remove unnecessary duplication in the system as we understand some payers routinely submit both a payment notice and a withholding notice at present where only one is necessary.
Clarification of the requirement that a section 110(2) payment notice should be served	<p>At present there is no clear link between the “sum due” under the contract and the amount notified in a Section 110(2) notice, this creates range of problems under contracts without certificates, as the payee does not have a clear entitlement to payment. <i>This measure brings the following benefits under these contracts:</i></p> <ul style="list-style-type: none"> ■ It will not be possible to withhold payment without notice. ■ It will be much clearer when the payee is entitled to suspend performance. 		<ul style="list-style-type: none"> ■ The current drafting of section 110(2) may lead the payer to conclude that he need not issue a payment notice because of certain deductions from the sum that would otherwise have been due.

Proposals	Benefits	Costs	Net Benefit
<p>Clarity of the Content of Payment and Withholding Notices</p>	<p>Our proposal creates a clear connection between the information in the section 110(2) notice and that required to withhold payment in accordance with section 111. This will remove unnecessary duplication in the system as we understand some payers routinely submit both a payment notice and a withholding notice at present where only one is necessary.</p> <p>Our proposal sets out a framework where a withholding notice should take the form of a revised payment notice. This single format creates clarity and simplicity, though in places additional information is required.</p>	<p>This proposal will increase the number of section 111 withholding notices that must be issued under contracts without certificates as the obligation is extended to all deductions. It is possible to estimate the cost to the construction industry of this change using DTI's estimate that 356,400 payments are made each year under contracts without certificates (40% of main contract payments and an additional 50% as an estimate for the number of payments made under sub-contracts).</p> <p>We are seeking responses from consultees on the proportion of payments that are subject to abatement after the payment notice deadline but, if it is one monthly payment every two and a half years, and the cost of a withholding notice is £25, we estimate that the additional inconvenience will cost the construction industry in England and Wales $356,400 \times £25 / 30 = \text{£}297,000$ per year.</p>	

Proposals	Benefits	Costs	Net Benefit
Clarity of the sum due	<p>By introducing much greater transparency about the sum due by providing a statutory definition. We believe this will:</p> <ul style="list-style-type: none"> ■ improve communication between the parties; ■ enable cash to flow down the supply-chain; ■ enable contractor to plan cash flow and address poor performance; and ■ potentially improve liquidity and reduce costs of servicing debt. 	<p>There will be an additional cost which will be borne by the payer as the Section 110(2) payment notice does not make it clear whether the payer needs to account for abatements and/or set-offs.</p> <p><i>This is an administrative inconvenience</i> which the industry has chosen to deal with by issuing separate notices under section 110(2) and 111.</p>	
Preventing 'pay when certified'	<p>Improves the predictability of cash flow and provides the supply-chain with a degree of certainty about what sum they will receive and when.</p>	<p>We understand that traditional civil engineering sub-contracts continue to include pay when certified clauses. DTI statistics suggest that 11,400 payments are made each year under civil engineering sub-contracts. As these will no longer become due under a pay when certified clause, the terms of the Scheme will apply and the payment will become due following the completion of the work or upon the issue of a claim by the payee, whichever is the later. The payer will then have to issue a payment or withholding notice. Assuming a main contract certificate has not been issued, this will require additional administration by the payer. Assuming a cost of £25 the total cost will be £285,000.</p>	<ul style="list-style-type: none"> ■ Improves communication between the parties; and ■ ensures money flows down the supply-chain

Proposals	Benefits	Costs	Net Benefit
Enhancing the existing right to suspend performance where there has been non-payment	<p>This proposal creates a statutory right for the payee to receive compensation for losses caused by the suspension.</p> <p>The payee will also have a sufficient length of time to remobilise on site.</p> <p>Threat of having to pay the additional costs of suspension incurred by the payee is intended to incentivise the payer to administer payment in a fair way.</p>	<p>This proposal does not introduce any overall increase in costs.</p>	<p>Suspension is a remedy of last resort and the current incidence of its use is low.</p> <p>The limitation to only loss and expense reasonably incurred makes the balance between enabling the payee to utilise the right to suspend and the new obligations which will fall on the payer a fair one.</p> <p>Prompt payment is essential to ensure an effective construction industry.</p>
Introduction of a statutory framework for the costs of the adjudication	<p>Greater access to adjudication for all.</p>	<p>Each party to a dispute is encouraged to be responsible for their own legal and other costs;</p> <p>Parties will also need to pick up the adjudicator's fees.</p>	<p>Legal and other costs will be kept low</p> <p>Prompt resolution of disputes.</p> <p>Still cheaper and quicker than going to court</p>

Proposals	Benefits	Costs	Net Benefit
<p>To prevent the application of “final and conclusive” clauses to interim</p>	<p>The joint DTI / CIC survey of adjudicators found that 50% of adjudication disputes relate to interim payments while the remainder relate to final payments or other matters. The survey also found that resolving payment disputes at the interim stage reduced the cost of adjudication by approximately 10%, or £2,000. This means that approximately 875 adjudications in England and Wales relate to interim payments.</p> <p>If adjudication of interim payments was encouraged by increasing the number that may be disputed from 418,200 to 492,000 (i.e. by 17.5%), this would represent an additional 150 interim payment adjudications. Compared to adjudication of the final account, this would result in an approximate reduction in the average cost of £306,000 or £175 per adjudication on average. Any arbitration or litigation cases that were also averted would increase this figure.</p>		
<p>Deleting the existing section 107 requirement that contracts need to be evidenced in writing</p>	<p>A large number of construction contracts contain orally agreed terms. Our proposal extends the application of the Construction Act to oral and partly oral construction contracts. Thus providing greater access to adjudication for more varied forms of construction contracts.</p>	<p>Responses to the joint DTI/CIC survey of adjudicators revealed that the additional complexity of adjudicating on oral contracts would not lead to a significant increase (<5%) in the cost of adjudication.</p>	

7. Small firms impact test

The proposed amendments will apply to all construction contracts within the scope of Part II of the Housing Grants, Construction and Regeneration Act 1996.

The legislation applies to contracts for construction work and professional services including mechanical, electrical, civil engineering and groundworks. A table showing some key statistical data on these sectors for England and Wales is set out below. These cover 2004 as this is the latest data available.

	Construction Contracting	Construction Professional Services	Total % of Whole Economy
Number of Enterprises	169,700	15,660	10.2%
% of small or micro enterprises	98.9%	98.8%	
Total Turnover	£136,800m	£9,400m	7.0%
Gross Value Added	£47,300m	£5,600m	8.1%
% of output** funded by public sector	30%	26%	
Average Employment	1,176,000	123,000	6.1%
Total Net Capital Expenditure	£2,950m	£150m	4.4%
Number of company insolvencies	1,653	Not available	13.6%*

* Based on contracting only

** Based on DTI output survey for contracting and CIC survey of construction professional services

Engagement of small firms

As with the previous consultation, the Department is once again inviting stakeholders of all sizes to voice their concerns/views either through their federations, trade associations or as individuals.

Given this general industry context, engagement of small firms, at all points in the supply chain, has been fundamental to the development of these proposals.

There have been a number of stakeholder events during the last eighteen months. Those attending have included construction trade associations whose main membership consists of small firms and other industry stakeholders. The National Specialist Contractors Council and the Specialist Engineering Contractors Group in particular have been very helpful in ensuring that representatives from SMEs attended these events (and in encouraging firms from within their membership to respond to the March 2005 consultation exercise). The purpose of these events has been to encourage those who would be affected by the proposals to voice their concerns and come up with suggestions for amending the Construction Act.

Among the many proposals considered, was whether “the payment framework under the Construction Act would benefit from the inclusion of a definition of what should constitute an adequate mechanism for payment?” The responses received to this suggestion indicated it would provide clarity for smaller firms and make clear on what date payment was due.

Likewise, support was also forthcoming for the proposal to “introduce a fallback provision should the payer not issue the advance notice of payment (Section 110(2) Notice)”. The payer is already duty bound by the existing legislation to notify the payee of the amount they will be paid and of any deductions being made.

The cost of monitoring cash flow, negotiating credit, as well as the financing costs and administration, information and legal cost involved in disputes can bear disproportionately on smaller businesses. Not only does this constrain development by increasing relative costs and reducing the ability of small businesses to compete but it can also divert resources from training, innovation and management.

Late payment is a particular issue for all in construction, particularly among SMEs. This is borne out from the most recent Small Business Survey, which reported that 46% of construction firms saw late payment as a major obstacle. It was also reported in the same survey that late payment also significantly had a detrimental impact on cash flow.

The survey also reported that 31% of construction firms have had to resort to the courts as a result of late payment.

The benefits of the proposed amendments to small and micro businesses are:

- introducing greater transparency and clarity into the payment framework to assist in the management of cash flow
- increasing access to a simple mechanism for resolving disputes
- improving communication between payer and payee on what will be paid and when
- encouraging prompt administration and communication of payment and improve the efficiency and productivity in the industry; and
- enabling the parties to continue to work together effectively to deliver high quality construction projects on time and on budget.

8. Equity and fairness

The gender mix of the UK construction industry is generally accepted as being dominated by white males, with women and ethnic minorities being under-represented.

According to the 2006 Labour Force Survey, there are approximately 800,000 self-employed individuals working in the UK construction industry of whom approximately 25,000 are black and minority ethnic or 3% of the total self-employed.

The proposed amendments to the Construction Act affect contracts between businesses and self employed individuals. They will apply equally to all businesses and individuals drawn from all ethnic groups, age groups and to men and women alike. Our proposals are unlikely to have a greater impact on any group as compared to another. The amendments all put in place regulatory reform that will remove burdens by:

- Improving the operation of the existing legislation by introducing greater clarity and transparency and reducing disincentives to use adjudication where appropriate;
- Help to maintain a level playing field in a competitive market with a large proportion of small firms; and
- Underpin existing best practice in the industry.

These amendments will better enable contractors to plan cash flow, address poor performance, and potentially improve liquidity and reduce the costs of servicing debt. They are intended to benefit small businesses in particular.

9. Competition assessment

The construction industry is extremely competitive. There is no dominant firm in the construction sector. Many firms report very low margins. Competition is healthy to the point of sometimes being extremely fierce affecting profitability.

Similarly, there is no small key group of dominant firms in any sub-sector other than perhaps some very small specialist feeds. The legislation does not set up barriers to entry to any sectors or to the construction industry and is unlikely to affect the size of firms or number, though it may reduce the churn brought about by the combination of insolvencies and new firms being established.

10. Enforcement, monitoring and sanctions

The DTI is not proposing to change the enforcement mechanisms introduced through the original legislation. The main enforcement mechanism for the legislation other than the courts or arbitration is the adjudication process, which the legislation provides. The decision of the adjudicator is binding on the parties and enforceable through summary judgement in court.

The only sanction being introduced is where an application for payment becomes due if the payer fails to issue a payment notice. No other sanctions are proposed.

11. Implementation and delivery plan

We are proposing to introduce the amendments through a Bill. Following an assessment of the responses to the consultation on the proposed amendments, we will introduce legislation as soon as parliamentary time is available.

12. Summary and recommendation

This package of measures strikes a fine balance between:

- the need to improve the effectiveness of the Construction Act by:
 - Improving the transparency and clarity in the exchange of information relating to payments to enable the parties to construction contracts to better manage cash flow; and
 - Encouraging the parties to resolve disputes by adjudication, where it is appropriate, rather than resorting to more costly and time consuming solutions such as litigation
- the important principle of not upsetting the compromise between all sectors of the construction industry which underpinned the introduction of the original legislation in 1996.

It is recommended that the proposed regulatory changes be proceeded with.

13. Declaration and publication

I have read the regulatory impact assessment and I am satisfied that the benefits justify the costs.

Signed

Date

Minister's name, title, department

Annex A – Proposals from the 2005 consultation on *Improving payment practices in the construction industry* which we are not taking forward

Trustee Accounts

In the consultation on *Improving payment practices in the construction industry* in March 2005 we proposed to amend the Construction Act to prohibit agreements that the payment resulting from an adjudicator's decision should be made into a trustee account. Responses to the consultation supported the view expressed by Sir Michael Latham that the clauses on trustee accounts make adjudication an ineffective means of securing cash flow. The analysis of the consultation in January 2006 explained (pages 26-27) that we intended to proceed with an amendment to the Construction Act to prohibit these clauses. It also noted that, on the basis of responses received, the use of these clauses was relatively rare with perhaps 1 in 100 construction contracts containing this kind of provision.

Subsequently, with its sounding board on amendments to the Construction Act, DTI concluded that the amendment should prohibit clauses that entitle the person required by the adjudicator to make payment to:

- withhold all or part of the payment;
- make all or part of the payment to a third party; or
- make all or part of the payment subject to any other condition,

...for any period or until the dispute is finally determined.

However, with its pre-consultation exercise with the Construction Umbrella Bodies Adjudication Task Group, DTI considered whether the current law already provides the courts with powers to strike trustee account agreements out of a construction contract when enforcing an adjudicator's decision. These agreements appeared already to be ineffective following the decision in *Ferson Contractors -v- Levolux AT* as a payment awarded by an adjudicator cannot be subject to set-off or deduction by the payer. The appeal court decision stated that an adjudicator's decision on payment should be enforced, even if it conflicts with an existing contractual right. The Construction Umbrella Bodies agreed with this view though they considered an amendment was still necessary.

With the passage of the Legislative and Regulatory Reform Act (LRRRA) 2006 we considered whether Ministers had the powers to implement this proposal under section 1 of the LRRRA. A Legislative Reform Order (LRO) must be for the purpose of removing or reducing any burden, or the overall burdens, resulting directly or indirectly for any person from any form of legislation. There appear to be two obstacles:

- The costs to the party denied payment under an adjudicator's decision results from the agreement made by the parties and not from the legislation. As a result it could not be considered a burden for the purpose of an LRO.
- More importantly, the proposal is caught by the precondition under section 3(2) (a) of the LRRRA which has to be met before a provision can be made under section 1. This is that "the policy objective intended to be secured by the provision could not be satisfactorily secured by non-legislative means". This reflects a broader principle which the DTI must bear in mind when legislating as cutting red tape and improving regulation is a key priority.

For these reasons, we have concluded that the most appropriate course of action is not to take forward a legislative proposal on trustee accounts either in an LRO or in primary legislation. It is more appropriate in the context of our emphasis on reduced burdens on business to rely on guidance to address this issue.

Annex B – Cabinet Office code of practice on consultation

The Code of Practice on Consultation sets out the basic minimum principles for conducting effective Government consultations. It aims to standardise consultation practice across Government and to set a benchmark for best practice, so that all respondents would know what to expect from a national, public Government consultation.

The six consultation criteria are:

1. Consult widely throughout the process, allowing a minimum of 12 weeks for written consultation at least once during the development of the policy.
2. Be clear about what your proposals are, who may be affected, what questions are being asked and the timescale for responses.
3. Ensure that your consultation is clear, concise and widely accessible.
4. Give feedback regarding the responses received and how the consultation process influenced the policy.
5. Monitor your Department's effectiveness at consultation, including through the use of a designated Consultation Co-ordinator.
6. Ensure your consultation follows better regulation best practice, including carrying out a Regulatory Impact Assessment if appropriate.

The complete code is available on the Cabinet Office website at:

<http://www.cabinetoffice.gov.uk/regulation/consultation/index.asp>

Comments or complaints

If you wish to comment on the conduct of this consultation or make a complaint about the way it has been conducted please write to:

Kathleen McKinlay

Better Regulation Team
Department of Trade and Industry
1 Victoria Street
London SW1H 0ET

Tel: 020 7215 2811

Fax: 020 7215 2235

Email: Kathleen.McKinlay@dti.gsi.gov.uk

Annex C – List of stakeholders

Construction Industry Council

Construction Confederation

National Specialists Contractors Council

Specialist Engineering Contractors Group

Technology and Construction Solicitors Association (TecSA)

The Construction Clients Group

Scottish Executive

Northern Ireland Assembly

Isle of Man Government

Others

This Consultation Document has also been sent to those who responded to the Joint DTI / Welsh Assembly Government consultation *Improving payment practices in the construction industry* published in March 2005.

See (<http://www.dti.gov.uk/sectors/construction/constructionact/page13956.html>)

Annex D – Consultation response form

We should be very grateful if you would answer these questions on the proposals in this consultation paper, and on their potential impacts. Please give reasons for your answers where you think it may be helpful. You should also feel free to suggest alternative approaches or make whatever additional comments or suggestions you think are appropriate.

Name

organisation

address

e-mail

Chapter 1 – Adjudication framework

1. Removing the requirement that the Construction Act should only apply to contracts in writing

- (a) Do you agree that Section 107 the Housing Grants, Construction and Regeneration Act 1996 should be removed so that the application of Part II of the Construction Act is not restricted to contracts where all the terms are in writing? **Yes** **No**

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.....
.....

- (b) Do you agree with us that the terms of an adjudication Scheme required by section 108 of the Construction Act should only be effective if agreed in writing? **Yes** **No**

.....
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.....

(c) Do you agree with us that the removal of the requirement that the parties must agree a contract in writing in order for the Construction Act to apply is unlikely to encourage the agreement of more oral or partly oral contracts? **Yes** **No**

.....
.....
.....
.....

(d) What proportion of contracts as a whole do you consider contain non-trivial terms which have been subject to oral agreement or variation?

- (i) 0% – 10%
- (ii) 10% – 25%
- (iii) 25% – 50%
- (iv) 50% – 75%
- (v) 75% – 90%
- (vi) 90% – 100%

Please select one from (i) to (vi).

(e) Do you agree with us that an agreement under paragraph 2 or 5(2) of Part I of the Scheme, as to who should act as adjudicator, should only be effective if agreed in writing? **Yes** **No**

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.....

2. Prohibiting agreements that interim or stage payment decisions will be conclusive

- (a) Do you agree that the Construction Act should be amended to prohibit agreements that decisions as to the amounts of payments whether by instalment, stage or other periodic payments are conclusive?

Yes No

.....
.....
.....

- (b) Do you agree that the prohibition of agreements that decisions are conclusive should include:

(i) Decisions as to the amounts of stage payments (i.e. for completed stages of work)? Yes No

(ii) Decisions which relate to the work that has been performed under the construction contract to the extent that it affects the amount of the payment? Yes No

...but that it should exclude:

(iii) Decisions as to the amount of final payment? Yes No

(iv) Payment decisions that have already been taken and notified to the parties? Yes No

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.....

3. Introduction of a statutory framework for the costs of adjudication

(a) Do you agree with our proposal to prohibit agreements as to the allocation of the costs of the adjudication until after the adjudicator is appointed?

Yes No

.....
.....
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(b) Do you agree with our proposal to provide that the adjudicator should have no jurisdiction as to the costs of the adjudication unless the parties have made an agreement to that effect after the adjudicator is appointed?

Yes No

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(c) Do you agree that adjudicators should be statutorily entitled to claim a reasonable amount in respect of fees for work reasonably undertaken and expenses reasonably incurred? Yes No

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(d) Do you agree that the courts should have jurisdiction to decide whether:

(i) The fees and expenses claimed by the adjudicator are reasonable when they are claimed under the proposed statutory right?

Yes No

(ii) The legal or other costs of the parties are reasonable when the parties have agreed that the adjudicator should make a decision as to legal or other costs and that the parties should be jointly and severally liable for this amount? Yes No

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(e) What proportion of contracts do you think contain an agreement that the referring party (or a specified party) should pay all or part of the costs of the adjudication?

- (i) Less than 0.1%
- (ii) 0.1% – 0.5%
- (iii) 0.5% – 1%
- (iv) 1% – 5%
- (v) 5% – 10%
- (vi) More than 10%

Please select one from (i) to (vi)

(f) What proportion of adjudications do you think are conducted under contracts containing an agreement that the referring party (or a specified party) should pay all or part of the costs of the adjudication?

- (i) Less than 0.1%
- (ii) 0.1% – 0.5%
- (iii) 0.5% – 1%
- (iv) 1% – 5%
- (v) 5% – 10%
- (vi) More than 10%

Please select one from (i) to (vi)

Chapter 2 – Payment framework

1. Prevention of unnecessary duplication of payment notices

- (a) Do you agree that the Construction Act should be amended so that a certificate from a third party supervising officer under a construction contract, which makes a valuation of the work done, may function as a section 110(2) payment notice? **Yes** **No**

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- (b) Do you agree that the Construction Act should allow the contract to provide that a section 110(2) payment notice may be issued either:

- (i) By the payer? **Yes** **No**
- (ii) By a person identified in the contract? **Yes** **No**
- (iii) By a person identified in a notice to the payee? **Yes** **No**

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- (c) Do you agree that the Scheme should provide that a payment notice under Part II paragraph 9 may be issued either:

- (i) By the payer? **Yes** **No**
- (ii) By a person identified in the contract? **Yes** **No**

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2. Clarification of the requirement that a section 110(2) payment notice should be served

(a) Do you agree that the drafting of the provision in section 110(2) of the Construction Act on when it is necessary to issue a section 110(2) payment notice should be improved to make clear that:

(i) a payment notice should be issued whenever the payment has been set-off, whether under another contract or the contract in question?
Yes **No**

(ii) allowance need only be made for abatement of the sum due under the contract in question and not another contract? **Yes** **No**

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(b) Responses to *Improving payment practices in the construction industry in 2005* suggested that a section 110(2) payment notice is only issued for 40% of payments. What proportion of cases where the notice is not issued do you think can be explained by the current deficiencies in the requirement in section 110(2) of the Act?

- (i) Less than 10% of cases where the notice is not issued (less than 6% of payments as a whole)?
- (ii) Between 10% and 33% of cases where the notice is not issued (between 6% and 20% of payments as a whole)
- (iii) Between 33% and 66% of cases where the notice is not issued (between 20% and 40% of payments as a whole)
- (iv) Between 66% and 90% of cases where the notice is not issued (between 20% and 54% of payments as a whole)
- (v) More than 90% of cases where the notice is not issued (more than 54% of payments as a whole)?

Please select one of (i) to (v)

3. Clarity of the content of payment and withholding notices

- (a) Do you agree that section 110(2) of the Construction Act should be amended to require that, in addition to the amount of the payment made or proposed to be made, and the basis of calculation, payment notices should also state:
- (i) the amount(s) withheld, where the payment is less than the amount that would have been due had the payee performed all his obligations under the contract and there were no set-off or abatement? **Yes** **No**
 - (ii) the grounds for withholding where amounts have been withheld? **Yes** **No**
 - (iii) the basis of calculation of any amounts withheld. **Yes** **No**
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- (b) If we introduce a requirement that payment notices should be in the format described above, do you agree that section 111 should be amended to require that withholding notices should be in the same format? **Yes** **No**
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- (c) Responses to *Improving payment practices in the construction industry* in 2005 suggested that a section 110(2) payment notice is only issued for 40% of payments. In what proportion of cases where the notice is issued do you believe it is later supplemented by a separate section 111 withholding notice because the payer is unclear about how the section 110(2) notice should act as a section 111 withholding notice?
- (i) Less than 10% of cases where the notice is issued (less than 4% of payments as a whole)?
 - (ii) Between 10% and 30% of cases where the notice is issued (between 4% and 12% of payments as a whole)
 - (iii) Between 30% and 70% of cases where the notice is issued (between 12% and 28% of payments as a whole)
 - (iv) Between 70% and 90% of cases where the notice is issued (between 28% and 36% of payments as a whole)
 - (v) More than 90% of cases where the notice is issued (more than 36% of payments as a whole)?

Please select one of (i) to (v)

4. Clarity of the “sum due”

(a) Do you agree that the Construction Act should be amended to ensure that the payer and the payee both know the sum due for the purposes of:

(i) section 111 – so that deductions (whether by set-off or abatement) can only be made from that sum by issuing a withholding notice?
Yes **No**

(ii) section 112 – so that they both know the amount that must be paid if the payer is to avoid the possibility that the payee will suspend performance? **Yes** **No**

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(b) Do you agree that this should be achieved by providing that:

(i) the sum due under a construction contract should be the amount paid or proposed to be paid as specified in a section 110(2) payment notice. **Yes** **No**

(ii) the amount in a claim by the payee should become due if no payment notice is issued. **Yes** **No**

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(c) For the purposes of this consultation, we have assumed that on average across the industry, one in 30 payments that are (or should have been) notified under Section 110(2) are later abated. Do you consider that this proportion:

(i) is about right?

(ii) should be less than half of this
(i.e. less than one in 60 payments)?

(iii) should be more than twice this
(i.e. more than one in 15 payments)?

Please choose one of (i) to (iii).

(d) Do you agree that the overall cost to the payee of securing payment under the payment framework in the Construction Act can best be measured as a percentage of each payment made under the contract?

Yes No

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(e) Notwithstanding your answer to question (d) what percentage of the amount of each payment finally due under a construction contract do you consider is lost on account of the cost and delay involved in obtaining proper payment?

- (i) Less than 1% of each payment
- (ii) Between 1% and 2.5% of each payment
- (iii) Between 5% and 10% of each payment
- (iv) Between 10% and 15% of each payment
- (v) Between 15% and 25% of each payment
- (vi) More than 25% of each payment

Please select one answer from (i) to (vi)

(f) If changes to the payment framework were introduced as proposed in this chapter, what percentage of the amount of each payment finally due under a construction contract do you consider would be lost on account of the cost and delay involved in obtaining proper payment?

- (i) Less than 1% of each payment
- (ii) Between 1% and 2.5% of each payment
- (iii) Between 5% and 10% of each payment
- (iv) Between 10% and 15% of each payment
- (v) Between 15% and 25% of each payment
- (vi) More than 25% of each payment

Please select one answer from (i) to (vi)

(g) If, as proposed, the sum due under a construction contract were to be viewed in law as the amount paid or proposed to be paid as specified in a Section 110(2) payment notice, (with the amount in a claim for payment becoming due if no notice were issued), what effect do you think this would have on the cost of resolving payment disputes at adjudication?

- (i) The cost would not be subject to a significant reduction (i.e. less than 5%)
- (ii) The cost would be reduced by 5% to 15%
- (iii) The cost would be reduced by 15% to 35%
- (iv) The cost would be reduced by 35% to 65%
- (v) The cost would be reduced by more than 65%
- (vi) The cost would be increased?

Please select one answer from (i) to (vi)

(h) Do you agree that the overall cost to the payee of securing payment can best be anticipated based upon recent experience of securing payments under:

(i) interim payment certificates following the introduction of the Construction Act; and **Yes** **No**

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(ii) the JCT "With Contractors Design" form of construction contract. **Yes** **No**

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5. Prohibiting the use of pay-when-certified clauses

- (a) Do you agree that the Construction Act should be amended to make clear that pay when certified clauses are not an adequate mechanism for determining when payment becomes due? **Yes** **No**

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- (b) Do you agree with our understanding that:

- (i) Pay-when-certified clauses are only used in Civil Engineering subcontracts? **Yes** **No**

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- (ii) Instalment, stage and other period payment decisions are not conclusive in any of the standard contract forms?
Yes **No**

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Chapter 3 – Improving the right to suspend performance

- (a) Do you agree that section 112 of the Construction Act should be amended to include a provision allowing the suspending party to claim a reasonable amount in respect of his costs caused by the exercise of the right to suspend from the party in default of payment (this would include the reasonable costs of remobilisation if this is required)? **Yes** **No**
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- (b) Do you agree that section 112 of the Construction Act should be amended to include a provision allowing the suspending party to claim an extension of time for meeting any deadlines in his contract with the party in default of payment for any delay to the completion of work caused by the exercise of the right to suspend? **Yes** **No**
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- (c) Do you agree that section 112 of the Construction Act should be amended to clarify that the suspending party may suspend any or all of his contractual obligations to the party in default of payment? **Yes** **No**
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- (d) What would you estimate to be the reasonable one-off costs of suspending performance on a typical construction project?
- (i) Less than 5% of an average monthly interim payment.
 - (ii) 5% to 15% of an average monthly interim payment.
 - (iii) 15% to 50% of an average monthly interim payment.
 - (iv) 50% to 100% of an average monthly interim payment.
 - (v) 100% to 200% of an average monthly interim payment.
 - (vi) More than double an average monthly interim payment.

Please select one of (i) to (vi)

(e) What would you estimate to be the reasonable monthly ongoing costs while in suspension on a typical construction project?

- (i) Less than 5% of an average monthly interim payment.
- (ii) 5% to 25% of an average monthly interim payment.
- (iii) 25% to 50% of an average monthly interim payment.
- (iv) 50% to 100% of an average monthly interim payment.

Please select one of (i) to (iv)

(f) What would you estimate to be the reasonable costs of remobilising performance on a typical construction project?

- (i) Less than 5% of an average monthly interim payment.
- (ii) 5% to 25% of an average monthly interim payment.
- (iii) 25% to 50% of an average monthly interim payment.
- (iv) 50% to 100% of an average monthly interim payment.
- (v) 100% to 200% of an average monthly interim payment.
- (vi) More than double an average monthly interim payment.

Please select one of (i) to (vi)

Do you consider that your answers to questions (d), (e) and (f) would be changed if the suspending party was not required to be ready to remobilise immediately, as at present, when the defaulted payment is eventually made, but was allowed an additional extension of time for any delay caused by the exercise of the right of suspension.

(g) Please select which of (i) to (vi) in question (d) you think would apply following the DTI's proposed amendment.

- (i) Less than 5% of an average monthly interim payment.
- (ii) 5% to 15% of an average monthly interim payment.
- (iii) 15% to 50% of an average monthly interim payment.
- (iv) 50% to 100% of an average monthly interim payment.
- (v) 100% to 200% of an average monthly interim payment.
- (vi) More than double an average monthly interim payment.

(h) Please select which of (i) to (iv) in question (e) you think would apply following the DTI's proposed amendment.

- (i) Less than 5% of an average monthly interim payment.
- (ii) 5% to 25% of an average monthly interim payment.
- (iii) 25% to 50% of an average monthly interim payment.
- (iv) 50% to 100% of an average monthly interim payment.

(i) Please select which of (i) to (vi) in question (f) you think would apply following the DTI's proposed amendment.

- (i) Less than 5% of an average monthly interim payment.
- (ii) 5% to 25% of an average monthly interim payment.
- (iii) 25% to 50% of an average monthly interim payment.
- (iv) 50% to 100% of an average monthly interim payment.
- (v) 100% to 200% of an average monthly interim payment.
- (vi) More than double an average monthly interim payment.

As well as covering the regulatory impact of the proposals described in this chapter on the costs of suspension, the following questions also cover the impacts of the proposal in Chapter 2 on the transparency of the sum due and its effect on right to suspend.

In reading questions (j) to (i) consultees should bear in mind the finding of improving payment practices in the construction industry that the right to suspend performance is exercised in fewer than one in a 100 cases of defaulted payment at present.

(j) Following the introduction of both:

- our proposals to reduce the costs of suspending performance in cases of non-payment; and,
- our proposals to improve the transparency of the sum due...

...how frequently do you believe the right to suspend performance would be exercised?

- (i) In more than one in five cases of defaulted payment?
- (ii) In between one in five and one in 20 cases of defaulted payment?
- (iii) In between one in 20 and one in 100 cases of defaulted payment?
- (iv) In fewer than one in 100 cases of defaulted payment? (i.e. no significant change)

Please select one of (i) to (iv)

(k) Following the introduction of only our proposal to reduce the costs of suspending performance in cases of non-payment how frequently do you believe the right to suspend performance would be exercised?

- (i) In more than one in five cases of defaulted payment?
- (ii) In between one in five and one in 20 cases of defaulted payment?
- (iii) In between one in 20 and one in 100 cases of defaulted payment?
- (iv) In fewer than one in 100 cases of defaulted payment? (i.e. no significant change)

Please select one of (i) to (iv)

- (l) Following the introduction of only our proposal to improve the transparency of the sum due in respect of the right to suspend performance, how frequently do you believe the right would be exercised?
- (i) In more than one in five cases of defaulted payment?
 - (ii) In between one in five and one in 20 cases of defaulted payment?
 - (iii) In between one in 20 and one in 100 cases of defaulted payment?
 - (iv) In fewer than one in 100 cases of defaulted payment? (i.e. no significant change)

Please select one of (i) to (iv)

- (m) What do you consider is the incidence of non-payment of a sum due in the construction industry?
- (i) Fewer than 10% of payments
 - (ii) 10% to 30% of payments
 - (iii) 30% to 50% of payments
 - (iv) 50% to 70% of payments
 - (v) 70% to 90% of payments
 - (vi) More than 90% of payments

Please select one of (i) to (vi)

- (n) What do you consider would be the incidence of non-payment following the introduction of both:
- our proposals to reduce the costs of suspending performance in cases of non-payment; and
 - our proposals to improve the transparency of the sum due?
- (i) Fewer than 10% of payments
 - (ii) 10% to 30% of payments
 - (iii) 30% to 50% of payments
 - (iv) 50% to 70% of payments
 - (v) 70% to 90% of payments
 - (vi) More than 90% of payments

Please select one of (i) to (vi)

(o) What do you consider would be the incidence of non-payment following the introduction of only our proposals to reduce the costs of suspending performance?

- (i) Fewer than 10% of payments
- (ii) 10% to 30% of payments
- (iii) 30% to 50% of payments
- (iv) 50% to 70% of payments
- (v) 70% to 90% of payments
- (vi) More than 90% of payments

Please select one of (i) to (vi)

(p) What do you consider would be the incidence of non-payment following the introduction of only our proposals to improve the transparency of the sum due in respect of the right to suspend performance?

- (i) Fewer than 10% of payments
- (ii) 10% to 30% of payments
- (iii) 30% to 50% of payments
- (iv) 50% to 70% of payments
- (v) 70% to 90% of payments
- (vi) More than 90% of payments

Please select one of (i) to (vi)

Chapter 4 – Other Issues which we are considering as part of this consultation

1. Devolution

- (a) Do you agree that the DTI and Welsh Assembly Government should continue to work together to minimise the differences between the effect of the provisions of the Schemes in England and Wales given that responsibility for the Scheme has been devolved to the Welsh Assembly?

Yes No

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- (b) Do you agree that, so far as is possible give the differences between Scots law and English law, the DTI and Scottish Executive should continue to work together to minimise the differences between the effect of the provisions of the Construction Act in England and Scotland given that responsibility for the Act has been devolved to the Scottish Parliament?

Yes No

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- (c) Do you agree that, so far as is possible give the differences between Scots law and English law, the DTI and Scottish Executive should continue to work together to minimise the differences between the effect of the provisions of the Schemes in England and Scotland? Yes No

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2. Correction of errors

- (a) Do you consider that the DTI and Welsh Assembly Government should work with the Scottish Executive to develop a “slip rule” with the intention, so far as is possible, of introducing the same rule in England, Scotland and Wales to ensure it is applied in a uniform way by the courts in England and Wales and in Scotland? **Yes** **No**

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- (b) Do you agree with the suggestion in the Scottish Executive’s report of its consultation on Improving adjudication in the construction industry that a slip rule should provide the adjudicator with:

- (i) Power to correct a clerical or arithmetic error or any other matter that the parties may agree... **Yes** **No**

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- (ii) for one week after the adjudicator’s decision or such longer period as the parties may agree? **Yes** **No**

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3. The Judgement of the House of Lords in Melville Dundas - v- George Wimpey

- (a) Do you agree that section 111 should not apply where the payee is insolvent, so that payment may be withheld without notice? **Yes** **No**

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- (b) Do you agree that sections 110 and 111 should apply in all other cases (i.e. to final payments as well as to “payments by instalments, stage or other periodic payments” which become due in accordance with section 109 of the Construction Act)? **Yes** **No**

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- (c) Do you consider that the judgement of the House of Lords in Melville Dundas -v- George Wimpey will have the effect which we have proposed the Construction Act should have in our view, when it is applied by the lower courts, so that:

- (i) Section 111 will not apply where the payee is insolvent, so that payment may be withheld without notice? **Yes** **No**

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- (ii) Section 111 will apply to all other grounds for withholding in respect of all payments (i.e. final payments as well as “payments by instalments, stage or other periodic payments” in accordance with section 109 of the Construction Act)? **Yes** **No**

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Please answer (Yes / No) to questions (i) and (ii)

(d) Do you consider that:

(i) the Act should expressly provide an exception to section 111 in cases where the payee is insolvent (section 113 already provides an example of an exception or insolvency), or leave this exception to be decided by the courts through case law following the House of Lords' judgement? **Yes** **No**

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(ii) the Act should be amended to make clear that section 111 should apply to all other grounds for withholding in respect of all payments (i.e. final payments as well as "payments by instalments, stage or other periodic payments" which become due in accordance with section 109 of the Construction Act)? **Yes** **No**

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