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## Construction Law Update:

### Late Payment – Is the Construction Act fit for purpose?

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## Introductions:

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## Late Payment – remains an ongoing issue

- + Payment has been an issue in the Construction industry for some time.
- + Prompt Payment Code.
- + Construction Payment Charter - a “dismal failure”.
- + Construction Act – 2011 amendments sought to improve payment.
- + A number of cases in the TCC considering the Construction Act.
- + 44% of contractors suffered non-payment due to insolvency alone in the last 3 years.
- + UK Government concerned that the Construction Act is not working.
- + Consultation on 2011 changes to Construction Act.



## Outline

1. Construction Act – Recap.
2. Examples of Construction Act not working.
3. Key points from recent case law in relation to the Construction Act.
4. Practical tips.
5. Keys to Payment under the Construction Act.
6. Other recent legislative attempts to improve late payment.
7. Consultation.
8. Our view.



## Construction Act – Recap (1)

- + Construction Act 1996 amended by LDED Act 2009 (“the Act”).
- + Statutory payment, suspension and adjudication regimes.
- + **Due Date** and **final date for payment** for any sum which becomes due.
- + Regime for providing **payment notices, by payer (client) or payee (consultant) not less than 5 days after due date.**
- + If the client required to issue the payment notice but does not:
  - **payee notice** before client’s payment notice due may be a “**default payment notice**”; or
  - payee may issue a “**default payment notice**”. Final date for payment is postponed between deadline for payment notice and submission of default notice.
- + If no valid notice – payment may not be due under the Act.
- + Framework for obtaining payment.

## Construction Act – Recap (2)

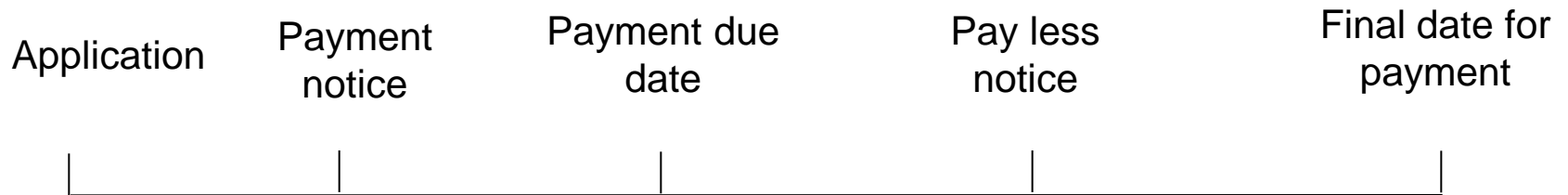
+ 2011 changes included:

- more detailed and more flexible payment notice regime;
- prohibition on pay when certified;
- statutory framework for the costs of adjudication;
- removing the requirement for contracts to be in writing; and
- improving the right of suspension.

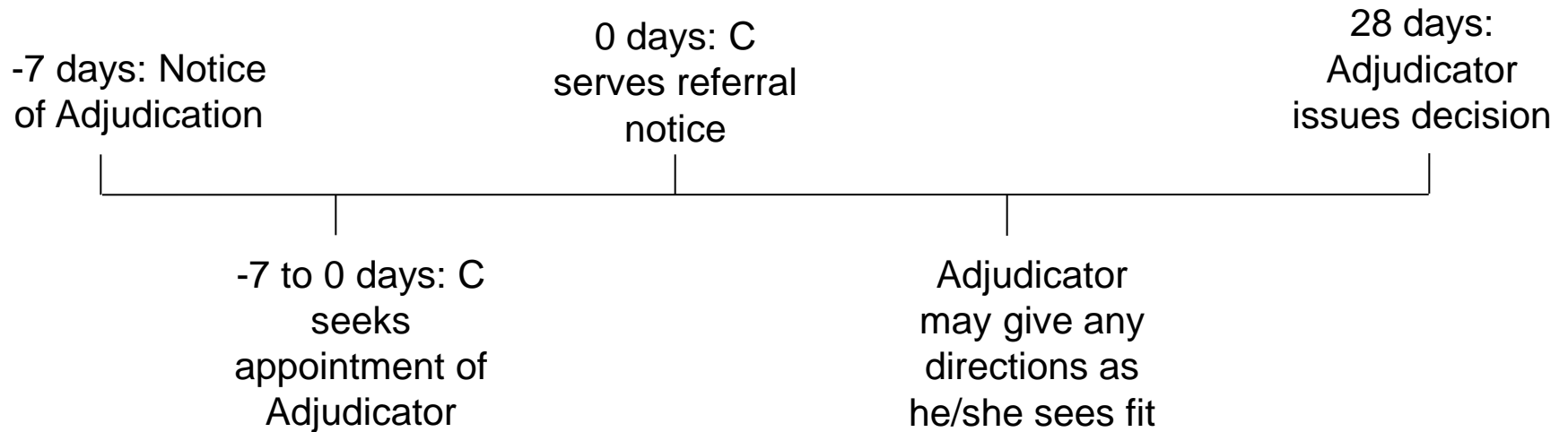
+ Positive changes.....

+ .....but did they work in practice?

## Typical payment procedure



## Typical adjudication procedure





## Examples of Construction Act not working

### **Payment:**

- + Overly complex payment regime - easy for technical breach.
- + Contracts often include additional requirements for sums to be due.
- + Pay when paid being operated in practice.
- + Payment often withheld until form of contract signed.

### **Adjudication:**

- + Abuse of the Adjudication process - T Clarke (Scotland) Ltd v MMAXX Underfloor Heating Ltd [2014].
- + Inappropriate forum for complex disputes i.e. professional negligence claims

## Recent Case Law

- + Significant number of recent cases in relation to the Construction Act.
- + Demonstrates the complexity of the payment and adjudication regimes.
- + Reveal “gaps” in the Construction Act.
- + We will now consider cases in relation to:
  - Right to Set off;
  - Contents of a Pay Less Notice;
  - Pay Less Notices and Final Applications;
  - Serial Adjudications;
  - “Smash and Grab” adjudications; and
  - Exceptions to the Act.

## Right to Set Off even if not given a Pay Less Notice

- + Pay less notice not a prerequisite of set-off defence.

### **DC Community Partnerships Ltd v Renfrewshire Council [2017]**

- + Following payment dispute, DC served notice of adjudication.
- + No pay less notice served.
- + Adjudicator failed to consider Renfrewshire's submission to set-off delay damages against any additional sums that the adjudicator might decide were payable.
- + Lord Doherty "*the Adjudicator was required to give at least some brief, intelligible explanation of why defence of set-off being rejected...*"
- + Renfrewshire's right to apply a set-off was not conditional upon a payless notice having been previously issued.
- + Adjudicator's decision not enforced.



## Contents of a Pay Less Notice



- + Important to draft clearly and set out basis sum considered due.

### **Muir Construction Ltd v Kapital Residential Ltd [2017]**

- + Pay less notice must specify the sum considered to be due and the basis on which that sum has been calculated.
- + Kapital issued pay less notice valuing the sums due at “zero”.
- + Held, notice “fell short of the requirements of the contract”. The pay less notice and supporting documents did not demonstrate the basis on which the assessment had been calculated.
- + Pay less notice must “at least to set out the grounds for withholding and the sum applied to each of these grounds with at least an indication of how each of these sums were arrived at”.

## Pay less notices and final applications

- + **Adam Architecture Ltd v Halsbury Homes Ltd [2017]**
- + HH emailed AA indicating that it will be using another architect but would still work with AA on house styles.
- + AA submitted a fee proposal for a full service and stopped work on the project, submitting an invoice for work to date.
- + No pay less notice.
- + HH was obliged to serve a pay less notice.
- + However... **Kilker Projects Limited v Rob Purton t/a Richwood Interiors [2016]** - the employer can adjudicate what is “properly due” at a later date.
- + Failure to issue a pay less notice in response to a Final Account may have limited consequences.



## Serial Adjudications

- + **Jacobs UK Limited v Skanska Construction UK Limited [2017]**
- + Skanska referred a dispute to adjudication and a timetable was agreed.
- + Skanska was unable to serve a reply by the required date and subsequently withdrew its referral.
- + Later, Skanska gave a fresh notice to refer the dispute to adjudication, containing the same claims but narrower in scope and with revised assessment for damages.
- + Jacobs claimed this was “unreasonable and oppressive”.
- + Held, Skanska’s withdrawal from first adjudication unreasonable - but did not justify preventing adjudication from proceeding.
- + However, Jacobs was entitled to its wasted costs caused by Skanska’s failure to comply with agreed timetable.





## “Smash & Grab”

- + Adjudicating on the basis of a technical failure to comply with the payment notice requirements under the Construction Act

### **ISG Construction Ltd v Seevic College [2014]**

- + ISG submitted an Interim Application for £1.1 million.
- + Seevic failed to pay sum or issue a pay less notice.
- + Despite the adjudicator agreeing that the works carried out were valued at £315,40,47, significantly less than £1.1 million, Seevic ordered to pay £1.1 million.
- + Amount claimed by ISG was due and payable.
- + However, “smash and grab” adjudications can significantly disrupt relationships on a project.
- + Courts emphasised need for payee to have complied with contract if relying on technical breaches by employer.

## Exceptions to the Act



### **Severfield (UK) Ltd v Duro Felguera UK Ltd (No. 2) [2017]**

- + Sub-contract was a hybrid with works included and excluded under s.105(2) of the Construction Act 1996.
- + As a result, court refused summary judgement on claim in relation to interim application for payment.
- + Parties ended up with two different regimes.
- + Described as "uncommercial, unsatisfactory and a recipe for confusion".
- + "the injustice to the claimant caused by Parliament's insistence on the exceptions [to the construction act]..has become even more apparent."
- + When construction act introduce adjudication was seen as a "punishment".
- + Now seen as a "blessing" by the construction industry so hopefully exceptions will be removed.



## Practical Tips

- + Consider limiting the client's right of set off to where a pay less notice has been given.
- + Take care when adjudicating in respect of a final application.
- + Pay Less Notices should clearly set out how the sum stated to be due has been calculated.
- + Beware of serial adjudications and seek to agree fixed timescales where possible.
- + Before any "smash and grab" adjudication review your position.
- + If contract is "Hybrid" include Construction Act payment regime.
- + Courts generally reluctant to look beyond agreed terms.

## Keys to payment under the Act

- + Does the Construction Act apply?
- + Application for payment (if any).
- + Payment Notice:
  - Content;
  - Timing;
- + Pay Less Notice.
- + Adjudicating for non payment.
- + Enforcing Adjudication.

## Construction Payment Charter

- + An agreement to apply fair payment commitments; be monitored for the purposes of compliance by reporting against a set of agreed KPIs; and consider the performance of the supply chain against the KPIs when awarding contracts.
- + Aim: 30 days & ZERO retentions.
- + Only 35 firms signed up to date including, just 3 main contractors and 2 private clients.
- + “The Charter has had no impact whatsoever. In fact while the Charter has been around payment periods have got worse stretching out to 50 days and 60 days.” – Rudi Klein CEO of Specialist Engineering Contractors’ Group.

## Reporting on Payment Practices (1)

- + Reporting on Payment Practices and Performance Regulations came into force in April 2017 requiring large LLPs and companies to report their payment practices and performance.
- + Applies to businesses that meet the thresholds published by the BEIS and “Qualifying contracts”.
- + Purpose: to improve late payment practices in the industry by highlighting who the “bad payers” are.
- + Significant information to be included in a report.
- + Reports need to be published at the end of each financial “reporting period”.
- + Failure to comply: criminal offence punishable by fine.

## Reporting on Payment Practices (2)

- + Are companies reporting?
  - Over 300 companies reported on their payment practices to date.
- + Is this having any impact?
  - Places an additional administrative burden on companies.
  - Likely to have limited effect on payment periods.
- + Reports can be published online at the following web address: <https://publish-payment-practices.service.gov.uk/publish>
- + Introduction of online database where suppliers can search businesses reports: <https://www.gov.uk/check-when-businesses-pay-invoices>

## Consultation (1)

- + BEIS has announced two consultations on the Construction Act:
  - + Review of 2011 changes to part 2 of the 1996 Act; and
  - + Review of the practice of cash retention in construction contracts.
- + First consultation seeks information on how effective the changes have been in securing their objectives by asking 51 questions that consider:
  - Issues such as access to adjudication, measures introduced to improve clarity and transparency of the payment framework;
  - Effectiveness of the 1996 Act and its fitness for purpose, the payment framework introduced in 2011 and the use of adjudication to resolve disputes; and
  - The affordability of adjudication and whether costs prevent parties from using it.

## Consultation (2)

- + Second consultation seeks information on the practice of cash retentions and considers:
  - How often retentions are paid late or not at all; and
  - The reasons for this.
- + The consultation also considers alternative methods such as, project bank accounts, escrow accounts, retention, performance bonds and retention deposit schemes.
- + Best way to influence consultations is to respond through the following two links:
  - <https://beisgovuk.citizenspace.com/im/2011-changes-to-part-2-of-the-housing/> and
  - <https://beisgovuk.citizenspace.com/im/retention-payments-in-the-construction-industry/>
- + Responses to both consultations due by 11.45pm on 19 January 2018.

## Our view

- + 2011 changes did improve the payment landscape.
- + The right to suspend under the Construction Act is particularly useful.
- + However late payment continues to be a real issue...
- + The payment regime can be useful but...
- + .... overly complex so requires very strong contract management.
- + “New payment provisions received some criticism for their complexity” – MCMS Director Jonathan Cope
- + The adjudication regime has been a success but too open to abuse.
- + Construction Act would benefit from simplification and strengthening.
- + An opportunity to improve late payment!



## Any Questions?

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