

Changes to the Construction Act.

Changes to the Construction Act 1996 (the Act) will come into force on 1 October 2011. The changes will apply to construction contracts and consultants' appointments entered into on or after that date.

The main changes relate to the payment provisions of such contracts and the paying party will now have to comply with a new regime of notices.

While the changes to the Act are not as extensive as was mooted in early consultations, the changes to the payment regime do require careful consideration. See below for our analysis of the key changes.

Introduction

Changes to the Construction Act 1996 will come into force on 1 October 2011. The changes will apply to construction contracts and consultants' appointments entered into on or after that date.

The main changes will affect payment. The existing regime of payment notices will be replaced by new notice requirements. It will now be even more important for payers to give the correct notices on time to avoid having to pay the amount claimed in a payee's application or a new payee's 'default' payment notice.

While a payee has always had a statutory right to suspend performance for non-payment under the Act, the changes significantly enhance this right, allowing the payee to suspend just some of his obligations rather than all of them - a right he might decide to use 'tactically' to suspend a crucial item of work - and to reimbursement of his reasonable costs and expenses.

Before 1 October it will be very important for clients to make sure that they and their teams (especially certifying architects and employer's agents) understand the new regime of notices and that their contracts comply with the new law. In anticipation of the changes to the Act, the JCT will be publishing a new suite of contracts later this month. Drafts of these contracts have already been issued.

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Background

The provisions of the Act are aimed at securing the flow of cash down the construction supply chain. To do this, certain compulsory payment provisions are required in all construction contracts and all contracting parties have a statutory right to refer disputes to adjudication (a fast-track method for resolving disputes). These provisions currently apply to contracts in writing for the carrying out (or arranging for the carrying out) of construction operations. The definition of “construction contracts” in the Act is wide: contracts caught by the Act include not only contracts for construction and engineering work but also demolition contracts, consultants’ appointments and development agreements which do not provide for the grant or disposal of a freehold or leasehold interest in the land on which the work is being carried out.

If a contract is caught by the Act and the parties fail to include the required provisions, the statutory Scheme for Construction Contracts (“the Scheme”) implies the relevant provisions into the contract. The Scheme is also changing on 1 October.

The main changes to the Act

Application of the Act

It will no longer be necessary for a construction contract to be in writing in order for the payment provisions of the Act to apply. Any contractual provisions as to adjudication must be in writing to be effective: if not, the adjudication provisions of the Scheme will apply. The JCT and many other contracts already opt for adjudication under the Scheme as it is generally considered to be fair to both parties.

Payment: the new regime of notices

It is to the payment provisions that the most substantive changes will be made. While the current requirements for an adequate payment mechanism and final date for payment remain, the existing regime as to payment notices is effectively replaced with new notice requirements so that:

- > For every payment made under the contract, a payment notice must be issued no later than 5 days after the “payment due date” (as stated in the contract). The notice must state the sum considered to be due and the basis on which it is calculated. This is similar to the current requirements but with some important differences:
 - whereas previously this notice had to be given by the payer, it can now be given – depending upon what the contract states - either by the payer or a “specified person” (such as an architect, engineer or employer’s agent) or the payee. Payers will want to retain the right to give the notice themselves or for their certifier to give it.
 - a payment notice must be issued even if the amount considered due is zero. Payers need to be careful therefore

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that notices are always issued on contractual due dates even if they consider there is nothing owing to the payee.

- > If the payer's (or his certifier's) payment notice is not given on time, the payee now has the right to issue a payment notice instead, stating what he considers to be due to him.
- > If the contract already permitted the payee to make an application for payment beforehand, that application is to be treated as the payee's notice and the payee is not allowed to give another notice. This is to prevent payees taking advantage of the fact that the payer has failed to give a payment notice on time by giving a second notice demanding more money than was stated in the payee's original application for payment.
- > The sum notified in a payment notice ("the notified sum"), whoever issues it, becomes payable before the final date for payment (subject to a "Pay Less Notice" being issued in time – see below).
- > The current system of "withholding notices" will be abolished and replaced by a new right for the payee to issue a "Pay Less Notice". A Pay Less Notice must specify:
 - the sum the payer considers to be due (even if zero) on the date it is served; and
 - the basis on which that sum is calculated.
- > The Pay Less Notice must be served no later than the number of days stated in the contract before the final date for payment. Where the contract is silent as to this period, the Scheme states that it must be served 7 days before the final date for payment.
- > The amount set out in the Pay Less Notice becomes the notified sum which the payer must pay.
- > Where a contract provides that the payer need not pay any sum due in respect of payment if the payee becomes insolvent and the payee becomes insolvent after the time limit for issuing a Pay Less Notice has expired, the payer can still withhold payment.

The new provisions for payee notices are obviously potentially dangerous for employers if they fail, or a third party certifier fails, to issue payment notices on time. The worst case scenario would be something like this: the employer/architect determines that for a particular payment claim no payment is actually due (for example, if the work is defective). However, no payment notice is given (remember, a payment notice must still be issued even if the amount considered due is zero). The contractor puts in his default payment notice for an inflated sum. Since the inflated amount is the "notified sum", this is the amount that the employer will have to pay if he does nothing further. However, he will still have an opportunity to issue a Pay Less Notice in relation to the amount claimed and in those circumstances it will be crucial for him to do so and to do so on time.

If the payer's notice is not given on time, the payee now has the right to issue a payment notice.

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Conditional payment provisions prohibited

“Pay-when-paid” clauses are already prohibited under the Act (except in the situation where the payer is not paid because of another’s insolvency further up the contractual chain, known as “upstream insolvency”). From 1 October, contractual terms which make payment conditional on the performance of obligations under another contract, such as “pay-when-certified” and “pay-what-certified” provisions, will also be banned, except in cases of upstream insolvency and where the contract is an agreement for the carrying out of construction operations by another person, for example, a management contract.

Enhanced suspension rights

If a sum due is not paid in full by the final date for payment and a Pay Less Notice is not given, the contractor may suspend his performance. As from 1 October, this right will be enhanced so that:

- > the contractor may suspend performance of just some of his obligations rather than all of them. Presumably this would be easier to do and could give him a powerful tactical tool (i.e. by threatening to suspend an important item of work).
- > the contractor will now be entitled to a reasonable amount in respect of his costs and expenses incurred (provided they are reasonably incurred) as a result of exercising his right to suspend. This would cover demobilisation, the period of suspension and remobilisation.
- > the contractor will be entitled to an extension of time for the delay caused as a consequence of the suspension (i.e. remobilisation) and not just for the period during which he suspends performance (as is his current entitlement).

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Adjudication changes

These are less extensive:

- > There is a new ‘slip rule’ which gives adjudicators the power to correct their decisions by removing a clerical or typographical error.
- > Contractual terms stating who is to pay the costs of an adjudication, regardless of the outcome, will be ineffective unless made in writing after the notice of adjudication is served. The contract can, however, give the adjudicator the power to determine which party pays his fees and expenses. If it does not do that and the Scheme applies to adjudications under the particular contract, the adjudicator now has the power to apportion payment of his fees and expenses but, regardless of that apportionment, if any amount remains unpaid, both parties are jointly and severally liable for the unpaid amount (as they always have been).

Contacts

For further information
please contact:

Huw Baker

Head of Construction

(+44) 20 7456 5180

huw.baker@linklaters.com

Kirstin Bardel

Counsel

(+44) 20 7456 3590

kirstin.bardel@linklaters.com

Author: Kirstin Bardel

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One Silk Street

London EC2Y 8HQ

Telephone (+44) 20 7456 2000

Facsimile (+44) 20 7456 2222

Linklaters.com